Six Steps to Building Trust and Engaging Shareholders
By Karen Kane

In these volatile times, how do you—as a company director—convey your competence in understanding the business before you, while also showing an appreciation for the gravity of your governance responsibility? A critical group of shareholders and a skeptical public are watching.

Quick, Mr. or Ms. Director, can you answer five key questions? Of course you will face many pointed questions over the next months, but these fivemay be most critical in establishingyour credibility:

1. Who are your top five shareholders?
2. How do shareholders view the company vis-à-vis the competition?
3. Can you explain the company's strategy in a sentence or a paragraph?
4. How well is management executing on the strategy? That is, how do you know, point by point, that management is creating long-term value for shareholders?
5. Can you explain the executive compensation program and why it is shareholder friendly?

Now more than ever, boards must convey how their work contributes to the strength and soundness of the enterprises they oversee. Consider that scrutiny of boards is on the rise as taxpayers have essentially become phantom shareholders through the public bailout of the private sector. Unlike shareholders who may be more educated about the role of the board of directors, the public at large may not understand the function—and value—of the governance role. How do boards of directors build trust in this era of greater accountability?

Increasingly, boards will utilize communication asan effective, strategic tool to build credibility and engage shareholders. Directors, however,must be prepared and educated on this front.As the season of annual meetings approaches, there is no time to delay. The shareholder meeting is a tremendous opportunity to transform what has long been a sparsely-attended pageant into a ripe opportunity to connect with shareholders.

Six Steps to Build Trust and Engagement with Shareholders

1. Don't Wait—Act Now (Build a Strategic Communication Policy)
The best practices endorsed by the National Association of Corporate Directors (NACD) and the Business Roundtable offer a template for boards to develop their own communication policy. There is no one-size that fits all. Rather, each board will want to establish its own guidelines. At the same time,developing the right message is highly situational: Is it business as usual, a major transaction or a crisis? By dividing communication into those three general buckets, boards can begin to coalesce their thinking.

By past practice and history, boards have not been externally focused. In fact, they have operated very quietly and below the public radar. Yet the financial failures of the past year have caused shareholders—and even now, the general public—to investigate how boards add value and whether they have remained true to their stated directives. Boards will find that education is a key element of communication, letting shareholders know what boards do—provide oversight—and do not do, namely manage the company. Nor should boards confuse communication with public relations. Boards are unlikely to ever undertake a PR campaign, but any board policy will acknowledge the current state of the external world. A board with a strategic communication policy can use transparency and communication as effective risk management tools. Conversely, a board with its head in the sand pretending that no one is looking is courting disaster or shareholder mistrust.

2. Engage an Independent Communication Advisor

Communication is not a primary board function. Over the years, most board communication has been informal, ad hoc and likely provided by the company staff. The world has changed. It is important for boards to have an objective outsider to help them craft a policyto anticipate and avoid crises, and to protect the company's brand. CEOs have come to see that a strong board enhances the leadership position and serves as an extension of the company's reputation. With each passing year, business success and sustainability have become increasingly dependent on reputation as word of mouth and third-party endorsements take on greater importance.

While legal counsel generally advises board clients to limit disclosure, the court of public opinion has changed the rules. In the face of shareholder activism, including majority rule and say on pay, boards face a host of very public issues. Whether it's a change in leadership, compensation issues or managing disclosure issuesabout the CEO's health, boards that have a written communication policy about how and what communication will take place are better equipped to navigate the waters more easily and with better results.

An independent communication counsel can help facilitate the board's adoption of guidelines to shareholders on the communication process and appropriate topics. Guidelines should also distinguish between management communication versus board communication.

Hiring board-level communications counsel is not a redundancy. Management's communication staff, including investor relations, does not speak for the board. A board communication resource separate from management's ensures the board's independence while retaining linkages with the company's values and strategies.

3. **Ensure Relevance and Timeliness—Use the Web**

Generally, board communication on the web is a static display of governance materials resulting in an impression that all boards are alike. As the financial world melted down in the final quarter of 2008 and continued its decline into early 2009, there waslittle indication on most board sites that anything dramatic had occurred.

There are a few exceptions.

A letter from the chairman and signed by the members of the Tellabs board begins, "*Dear Fellow Shareholders, In a year in which we collectively have experienced the largest financial shock since the Great Depression, shareholders have naturally focused on the governance and management of the companies in which they invest.Tellabs has a talented management team, a sound strategy, and the discipline to execute in a market that continues to grow and change…*" Tellabs' statement was among only a small handful of board-level communications willing to address the current crisis clearly and honestly.

4. Use the Compensation Discussion and Analysis (CD&A) to Convey a Shareholder-Friendly Philosophy

The Security and Exchange Commission mandated that public companies thoroughly explain their executive compensation practices. In practice, this disclosure is burdened by excessive legalese, complexquantitative models, and difficult-to-follow analysis; all of this serves to confuse rather than clarify the board's approach to rewarding management. Begin with a one-paragraph description of the compensation philosophy, then use the tools of a journalist—table of contents, headlines, bullets, summaries and callouts—to provide the details. These narratives must be written for your shareholders at a level that assumes some baseline knowledge of the financial markets and business practices—but definitely not written expressly for the SEC professional. While the document satisfies an SEC requirement, it should be targeted to an educated layperson.

5. Communicate to All Shareholders the Path of Shareholder Petitions

Even shareholders who are not involved in a specific shareholder petition should know and understand the process of making suggestions to the board and how the company responds.

Shareholders are not a monolithic group but rather represent many points of view. Nor should shareholders be encouraged to believe that they can micromanage the company. The board should take shareholder suggestions into consideration, but ultimately board oversight is not a democracy. Boards are called upon to be stewards, to bring their experience and business judgment to their role.

6. Make This Year's Annual Meeting an Effective Platform for Communication

Take a page from Warren Buffett's playbook. No, it will not require renting the Qwest Center to prepare for 31,000 shareholders or answer questions for six hours, but directors should use the meeting as an opportunity for stronger shareholder engagement. Many boards are finding value in interacting with key shareholders on a quarterly basis—whether through a phone call after the earnings call or other related tactics. It is clear the journey back to a 14,000 Dow and historic share prices will be a long one, and keeping shareholders invested in the company's strategy and plans has value.

After operating behind closed doors for so long, boards may find no better time than the annual meeting to share its communication policy with shareholders. The most important act for board members may be listening.With advance preparation, board members—particularly the lead director or chairman as well as chairs of the audit, compensation and nominating committee—should be available to take questions.

Webcasting the proceedings also increases transparency and inclusion. Posting the webcast on the website adds tremendous value and signals a move to greater openness.

Transparency and communication serve as risk mitigation strategies for the company and the board. It's an opportunity of limited duration. Smart directors will take the lead in acting now.

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