THE GREAT BOARD REBOOT

Board members open up on changing roles and expectations

FINANCIAL TIMES

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THE NEW BOARD AGENDA

In the wake of corporate scandals, a global pandemic and an uncertain economic and social recovery, all eyes are firmly on the board. Beyond regulation and compliance, board members must be able to detect risk and opportunity like never before.

Amid greater accountability and governance reforms, boards have to be more flexible, more agile and more responsive.

“Boards have to show the sort of leadership that pulls the best of their organisations’ people and thinking into play,” says John Elkington, who has served on more than 70 boards and advisory boards. “The best ones do exactly that — they are made up of people who are curious and committed – and who understand that the world changes, often in unexpected ways.”

This report, which is based on the findings of a global survey of more than 600 Financial Times readers who currently sit on boards, as well as interviews with leading experts, reveals how directors are embracing this evolution in their role and responsibilities.

It finds that the role of the board director is undergoing profound change. Individual and collective expectations are rising. The way that directors are recruited, trained and developed is being reshaped. And the composition of the board and the breadth of its expertise is under intense scrutiny.

The board agenda has always been packed. Now it comes with added complexity.

SECTION ONE:

RISK, REWARD AND RESPONSIBLE BUSINESS

Our research was carried out in the long shadow of Covid-19, so it comes as no surprise that disruption and uncertainty weighed heavily on the minds of board directors. The pandemic required many businesses to change their strategies almost overnight, which placed more responsibility, scrutiny and pressure on board process and procedure.

Which of the following are the greatest strategic challenges facing the board you sit on?

Based on the net top three challenges chosen

1. Economic volatility/uncertainty
2. Adapting organisation to a new business/operating model
3. Increasing business risks (e.g. climate change)
4. Composition of the leadership team
5. Changes to corporate governance rules/regulation

It also saw a higher number of board-level changes as businesses sought the right experience to respond to the crisis.[1]

"Covid-19 has forced boards to examine their organisations' business models and to anticipate disruption proactively," says Nayantara Bali, an independent director of StarHub and a non-executive director of Inchcape. "For businesses facing disruption, it's how we deliver the numbers, how do we reinvent the business, while at the same time worrying about governance and the environment."

Identifying new and emerging threats has always been part of a board's oversight role, but it is becoming a defining skill. When asked in which area they would personally welcome more insight and guidance, half of board members say new approaches to risk management.

Sam Mostyn, president at Chief Executive Women and chair of Ausfilm, says that the scale of the Covid-19 crisis took risk management strategy to another level.

"Pandemics were probably on most risk registers or radars of large companies," she says. "But the ubiquity of Covid-19 means that directors have had to think very differently about what risk management looks like when all the things you have relied on to run the company are removed."

According to the findings of an EY report on board risk, directors should "get comfortable with discussing risk more frequently."[2] Independent Audit's practical guide to principal risk management says boards should "test the logic" of their approaches:[3] "Each risk should have meaning. And it should lead to development of a risk management response, with actionable steps that can be monitored."

Mostyn says the pandemic has changed the intensity and scope of risk management discussion. "The boards I sit on probably met at least twice as many times during the Covid-19 period than previously," she says. "We have had to get very good at understanding the new forms of risk that occur when a catastrophic set of events changes the very nature of your business."

"The ubiquity of Covid-19 means that directors have had to think very differently about what risk management looks like when all the things you have relied on to run the company are removed."

SAM MOSTYN,
PRESIDENT AT CHIEF EXECUTIVE WOMEN AND CHAIR OF AUSFILM

Progressive boards ask unpopular questions

The changing social and business context of the past year is reflected strongly in how respondents see the evolving role of the board. Close to three quarters (72 per cent) agree that board members require a much deeper knowledge of company operations and competitors than ever before.

As three-year strategy cycles become a distant memory, boards need to operate within a much more flexible framework.

Randall Peterson, professor of organisational behaviour and academic director of the Leadership Institute at London Business School, says this calls for a more dynamic board. “We want boards to be much more active, more probing, to have a better understanding of how the business operates, to ask better questions in the boardroom.”

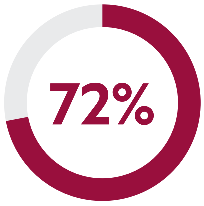
More than three quarters of board directors (77 per cent) say that boards need to make more time on the agenda to discuss innovation and strategic growth. But are members fully equipped to take their businesses forwards? The research finds that two of the traits most lacking among board members are ‘visionary’ and ‘progressive’.

Lucy Marcus, non-executive board director, and professor of leadership and governance at IE Business School, says that these qualities are vital: “Every board agenda has to have the right balance between grounding (legal requirements and regulation, audit, financials, the risk register) and stargazing — the questions of strategy ‘Where do we want to be in five, 10, and 15 years’ time?’ ”

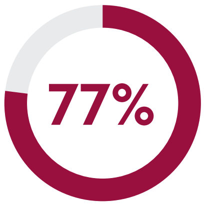
Peterson agrees that being progressive is critical, and that the traditional, finance-oriented way of thinking about boards is not enough. “What do board members add to the organisation? Yes, they must make sure that mistakes are not made, but what is their value beyond that? How do they consult, advise and make useful connections?”

A recent article in Harvard Business Review outlines 10 questions board members should be asking in order to be proactive.[4] These include, “What don’t you know about the company that you’re most concerned about?” and “What is the executive not telling you that you feel you need to know?” The premise is that asking such questions “may not make you popular ... but they can enable change at the level of individual board members and the board as a whole”.

John Elkington says that, when you look at poor board decisions of the past, the root cause is often an easy consensus. “This is because we like to be comfortable. It takes a rare board-level player to really stand up for major changes, but these people should be celebrated.”



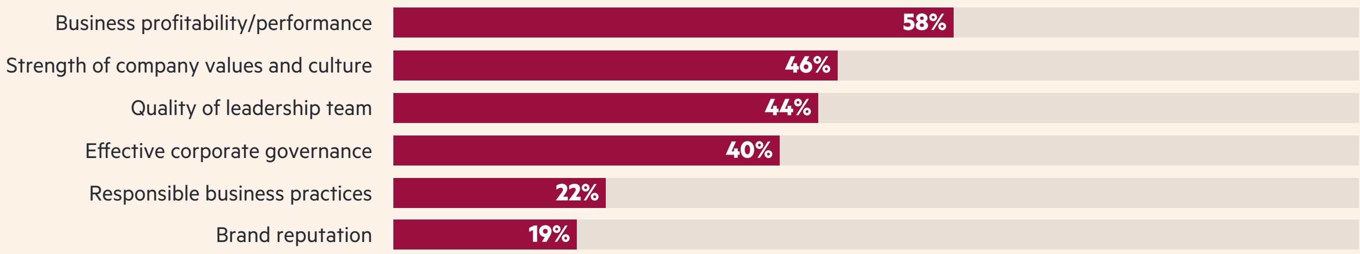
agree that board members require a much deeper knowledge of company operations and competitors than ever before



agree that boards need to make more time available to discuss opportunities for innovation and strategic growth

BEST WAYS TO ASSESS BOARD PERFORMANCE

Which of the following are the most e ective measures for judging board performance?



The new metrics of success

The traditional remit of the board is being given a contemporary makeover. But what does that mean for how a board is evaluated? The traditional indicator of a board's success — company profit — still comes out on the top as respondents' most effective performance measure. But other indicators are becoming increasingly important: company values and the quality of the leadership team are cited by nearly half of respondents, and two out of five say that effective corporate governance is a key measure.

Ruth Medd, chair of Women on Boards, adds another: enthusiasm. "Is the business thriving? Are people enthusiastic? Do board members walk around and chat to people? Do they go on site visits?" she asks. "Is there enthusiasm for the board itself?"

Performance measurement can be tied closely to the issue of board balance. "My first test is to look at whether it is a diverse board with the right mix of skills and competencies represented around the board table," says Sam Mostyn. "And, if not, why not? An investor will ask the question: 'How can that group of people carry out that fiduciary duty to investors if they have a particular set of blind spots by virtue of their homogeneity?' "

In its wide-ranging report on The Ethics of Diversity, the Institute of Business Ethics says that "the opportunity to tap into a broader reservoir of cognitive and experiential diversity has not yet been maximised".[5]

Beyond financial metrics, there are various means by which the performance of the board will be assessed. These include shareholder dissent and activism; the number and pattern of disclosures; the level of regulatory intervention; and, of course, the quality of the leadership team.

Is the board trusted to select the chief executive who can set and execute a strategy that will have been influenced by the pandemic? For 44% of respondents, the quality of the leadership team is one of the most effective measures by which to assess board performance. Others look to external measures to assess investor sentiment. In Australia, companies use the Corporate Confidence Index[6] to gauge the strength of governance over time.

About a fifth say that responsible business practices are an effective performance measure. However, a recent survey by London Business School/PwC found that almost half of FTSE 100 companies have linked executive pay to ESG targets. About a third have an ESG measure in their bonus plans, and a fifth include such targets in their long-term incentive plans.

Nayantara Bali expects this trend to continue. "In future, ESG will be a metric by which we can judge whether boards are doing well," she says. "The kinds of decision that need to be made to make progress on ESG metrics will typically be board-level decisions."

Issues related to social inequality and protection of the environment cannot be ignored by business. In the UK, there is growing momentum behind a campaign to change UK company law, to "ensure businesses are legally responsible for benefiting workers, customers, communities and the environment, while delivering profit."[7]

"Since the pandemic hit, people are talking more about areas that were not formally part of most board agendas previously, such as wealth divides, access to medicine, public health care and tax issues," says John Elkington. "If there is an understanding that this is a systemic set of challenges, that is a major step forward."

Sam Mostyn agrees that sustainability and social issues are rising up the agenda. "Boards I serve on take very seriously the notion of sustainability and long-term value creation," she says. "And ESG questions from shareholders have rocketed up in terms of prominence — questions around the ability to transition to low carbon, removal of waste from supply chains and issues of modern slavery within our procurement and supply systems."

"The kinds of decision that need to be made to make progress on ESG metrics will typically be board-level decisions."

NAYANTARA BALI, INDEPENDENT DIRECTOR OF STARHUB AND NON-EXECUTIVE DIRECTOR OF INCHCAPE

Climate change hits home

For many boards, it is global supply chain disruption that has brought the importance of ESG into sharp focus. This is pandemic-induced in many cases, but is also increasingly related to climate issues.

Ahead of November's COP26 meeting, pressure on CEOs and boards to act on climate change is intensifying. The recent vote by ExxonMobil's shareholders to change its board and the instruction for Royal Dutch Shell to cut its emissions faster are just two examples.

"Whether you are in Australia, California or Brazil, businesses are being affected by climate change and the depletion of natural resources," says Elkington. "The disruptions of supply chains have started to impinge on our capacity to do business, just as people are beginning to think about deglobalisation. This is concerning at a time when we need global responses to global problems. But what's also quite striking is that many of the insurgent businesses that are challenging the incumbents are intrinsically more sustainable."

These issues affect day-to-day business but also the liability of board members. Sam Mostyn says there is now a climate change fiduciary duty. "You need to show you are competent in understanding the climate risk to the organisation and how the company mitigates that."

More stakeholders have their say

The survey finds that this changing nature of governance is a concern: 36 per cent of respondents agree that boards are finding it hard to adjust to the multi-stakeholder model. Boards now have to consider more than just the shareholders. Can they rise to that challenge?

"You have to love governance — you cannot just retire into board life," says Mostyn. "Good directors have personalities and a view of the world, and they take very seriously their obligation to carry out that fiduciary duty more broadly than just a straight relationship with the investors." Mostyn says that, along with capital management and strategy, the "cultural underpinnings of the organization have become a primary responsibility of boards holding management to account on these issues".

"I think the next two years are going to be absolutely critical in terms of ESG," says Elkington. "Some boards will get it right, but a lot will find it is too complicated and will try to dilute or even drop it. By 2030 I think we will have seen a profound, seismic shift in the makeup of boards — not necessarily lots of sustainability experts, but people who are open to that agenda, connected with people who are active in that world, and bringing the new agenda into the heart of the business."

"By 2030 I think we will have seen a profound, seismic shift in the makeup of boards — not necessarily lots of sustainability experts, but people who are open to that agenda."

JOHN ELKINGTON

The new board: younger, broader minded, more accountable?

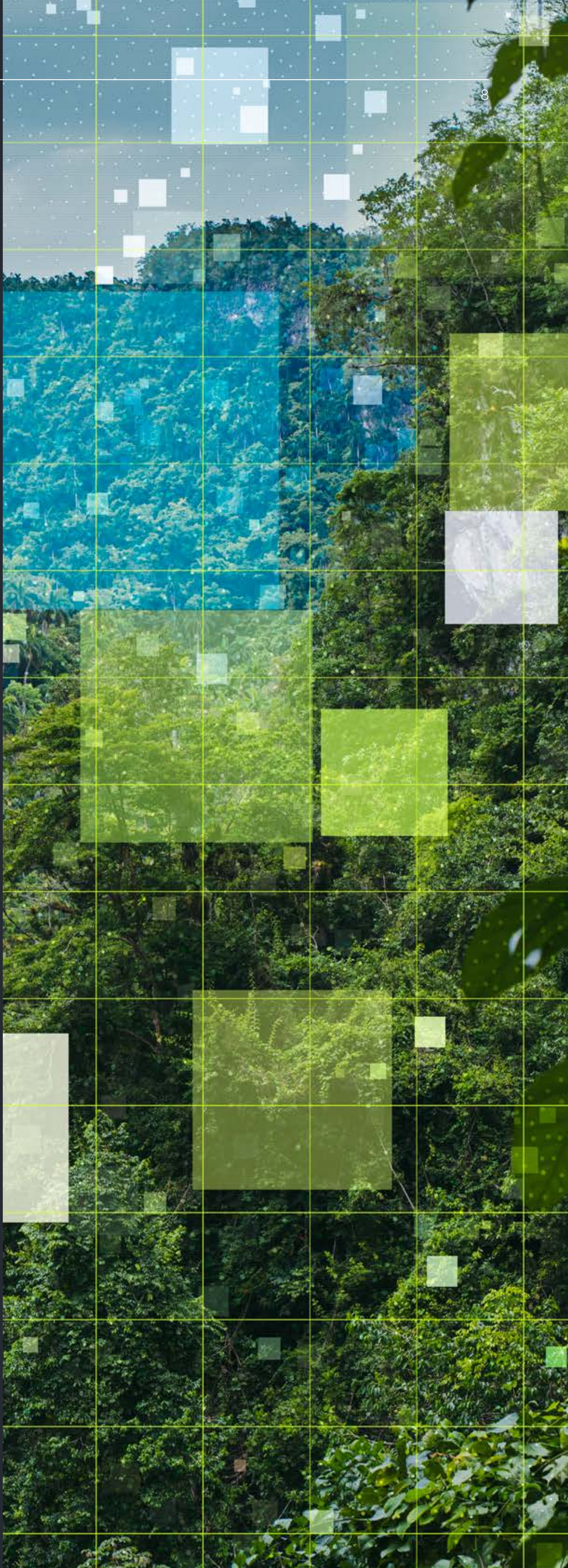
Responses to our question about the biggest changes to board governance over the next two years reinforce the idea that the make-up of the board will change. More than a third of respondents believe that more younger members will join boards.

"Younger execs are keen because they are passionate about ESG, diversity and governance, and believe they can have an influence," says Bali. "That interest in board positions wasn't there when I first joined a board."

John Elkington agrees. "These individuals are sustainability natives in the sense that they see the challenges, this is very much their future, and they want to see them being addressed properly and effectively, and in a timely manner."

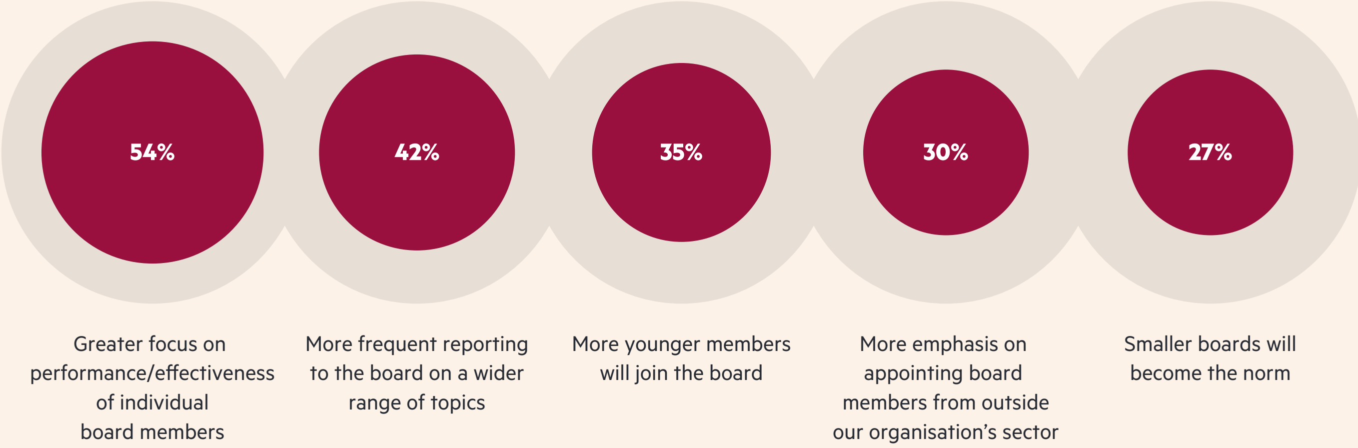
Such impetus has seen the rise of 'shadow boards', often a group of younger employees who help to shape company strategy on issues such as digital transformation.[8]

There remains, however, some way to go. Research from Spencer Stuart in 2020 suggests that the average age of a non-executive director in the FTSE150 is 60.3.[9] Among the new directors, 32% (51) were joining the board of a listed company for the first time.



GREATEST CHANGES TO BOARD GOVERNANCE

In which of the following ways, if any, do you expect the model of board governance to change over the next two years?



More than half (54 per cent) say there will be a greater focus on the performance of individual board members. "Individual accountability of board directors will increase," says Lucy Marcus. "Up until now, a board director can take a vote on something, walk out and say, 'Well, I tried to be supportive of the measure, but what can I do?' That will not be sufficient."

Indeed, a study by the EY Center for Board Matters found that nearly half of Fortune 100 companies disclosed that they had conducted individual director evaluations in addition to board and committee evaluations.[11]

Other areas of likely change include more frequent reporting to the board on a wider range of topics (42 per cent), and more emphasis on appointing board members from outside the organisation's sector (30 per cent).

Expanding the board's horizons is something that John Elkington says will be a crucial challenge.

"Stakeholder capitalism is not simply guessing what your stakeholders want — particularly external ones. It is delivered by pulling them in and getting them to act as a new sort of customer, injecting their priorities into your organisation. Bring the outside world in and also get your people out: take them as a group to places in the world where the future is already evolving."

> "Up until now, a board director can take a vote on something, walk out and say, 'Well, I tried to be supportive of the measure, but what can I do?' That will not be sufficient."
>
> LUCY MARCUS,
> NON-EXECUTIVE BOARD DIRECTOR,
> AND PROFESSOR OF LEADERSHIP AND GOVERNANCE AT IE BUSINESS SCHOOL

SECTION TWO:

DIVERSITY — A WORK IN PROGRESS

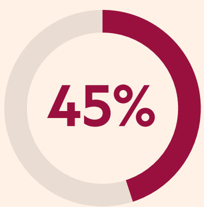
One aspect that many experts agree on is that effectiveness comes from the construction of a well-balanced board. But the survey findings on diversity are mixed: although progress has been made, there is still a long way to go to enable fair representation.

Nearly half of respondents (45 per cent) agree that their boards have been successful in appointing members from a wide variety of professional and personal backgrounds, but 40 per cent say their boards need much greater diversity among their members.

In the UK government-backed Parker Review into corporate diversity on FTSE 100 boards, almost a fifth were found to have no ethnic minority representation.[12] This is a significant improvement from a year earlier, when about half had no minority representation, but it falls short of the "one by 2021" target set for all FTSE 100 boards by the Parker Review in 2017. According to research from Heidrick & Struggles, 51% of new FTSE 350 boardroom directors were women.[13]

When it comes to gender, the research finds that 40 per cent of respondents think that greater gender diversity of boards improves performance. So, by not diversifying boards, companies are not only failing to fairly represent the society they operate in, they are also setting themselves up to underperform.

"Boards where there is a commitment to gender diversity and equality are telling a story about their commitment to representing the communities in which their companies operate," says Sam Mostyn. "In my experience, the ability of those boards to manage complexity and see things from different angles is far stronger than those that have not yet built enough of a presence of women."



agree that their boards have been successful in appointing members from a wide variety of professional and personal backgrounds

But

say their board needs much greater diversity among its members (age, race, educational background, culture, experience and gender)

And

agree that greater gender board diversity has improved the performance of their organisations

The next challenge, says Mostyn, is to address the lack of cultural diversity on boards: "Increasingly, our superannuation pension funds are asking the question of gender and cultural diversity presence on boards and putting it up front as a question as to if not, why not?"

According to Heidrick & Struggles, the share of racially and ethnically diverse appointments on Fortune 500 company boards has grown. But separately, EECO data suggests that black Americans still hold only 3 per cent of executive or senior level roles in companies with 100 or more employees.[14]

The picture in Europe appears mixed. In its latest Board Monitor report, Heidrick & Struggles[15] concludes: "In terms of racial or ethnic diversity, almost all boards in Europe could do better. In this context, we believe it's crucial that boards not trade off one form of diversity for another, and instead ensure that there's room in the room for everyone."

Is such sluggish progress down to how an organisation appoints its directors? Ruth Medd says that some companies are more proactive than others in diversifying their boards: "One of the barriers to diversity on boards is the way that directors are recruited. Many board roles are still filled through networks of board directors rather than through professional searches and recruitment processes."

Companies that have used a tried and trusted set of executive search firms and head-hunters will consider a more strategic approach, which includes appointing specialists.[16] They should also, according to the Institute of Business Ethics, be bold in setting criteria for board appointments and "push their executive firms to generate candidates well beyond the usual boundaries".[17]

Even if companies are successful in appointing directors from a breadth of backgrounds, they still have to work hard on creating the right culture and dynamics in the room.

"Do they collaborate? Do they avoid groupthink? Do people with different perspectives feel like they can contribute?" asks Randall Peterson. "It sounds simple, but it's actually very hard for boards to do."

"One of the barriers to diversity on boards is the way that directors are recruited."

RUTH MEDD,
CHAIR OF WOMEN ON BOARDS

Women on Boards: Cause for optimism?

Women on Boards was founded in 2005 and is now a global network of 60,000 women, and some men, with all levels of board experience, across all sectors and professional disciplines.

“Our objective from the very beginning was, and still is, to get reasonable representation of women on to boards at 40/40/20 — so 40 per cent women, 40 per cent men and 20 per cent of either,” says Medd. “We also started to focus on developing the careers of women, providing the pathway to becoming a director, or moving on to bigger and better boards.

“We had to enable women to understand what being a board director is about and how you might become more appealing to boards who are looking for directors,” she adds. “We are also a hub for board roles to our members.”

In Australia, Medd believes that many organisations are getting close to the Women on Boards goal of equal representation.

“We have collected data on the number of women on boards across categories including ASX 200, ASX 300, universities, government departments, credit unions and sports bodies, and there is steady improvement from 2010 onwards,” she says. “Some areas are doing quite well — most government boards, for example, are up to almost 50 per cent. ASX 200 is up to about a third. So I am quite optimistic — progress has been made.”

SECTION THREE:
THE BOARD PROFESSION

As the nature and make-up of boards change, so do the demands placed on their members. The research highlights a number of areas where board directors feel they need to improve their knowledge.

They include intelligence on emerging competitors and awareness of new workforce models, as hybrid working becomes the norm.[18] A greater understanding of the impact of digital technologies is cited most often.

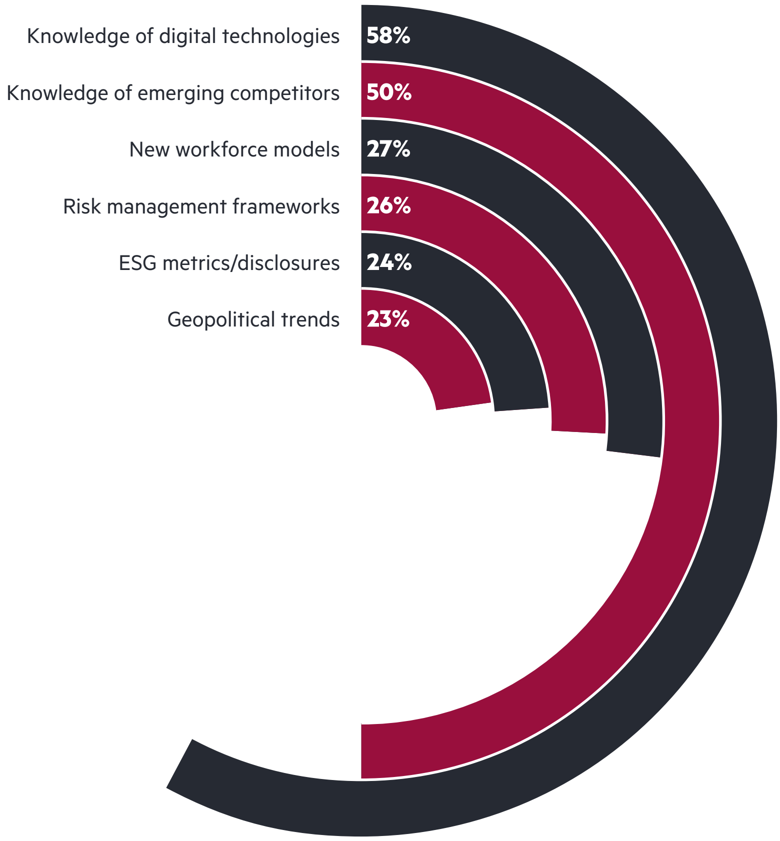
The latter is little surprise given that, according to EY research, two of the leading risks most cited by boards and CEOs to impact their organisations are cyber-attacks and the pace of technology change.[19] A recent survey by the IoD[20] found that a third of company directors said that their organisation was more exposed to cyber threats.

“The problems boards are trying to deal with are more complex than ever — the demands are growing,” says Randall Peterson. “It means boards have to be much more responsive to a broader set of stakeholders – and the outside world – than they have been before.”

Such complexity has seen boards recruit independent directors with specialist skills in areas such as cybersecurity, sustainability and diversity. While the ongoing impact of the pandemic has seen calls for boards to recruit public health experts.[21]

CLOSING GAPS IN BOARD KNOWLEDGE

In which of the following areas do you most need to improve your knowledge to become a more effective member of the board?



Contrary is welcome

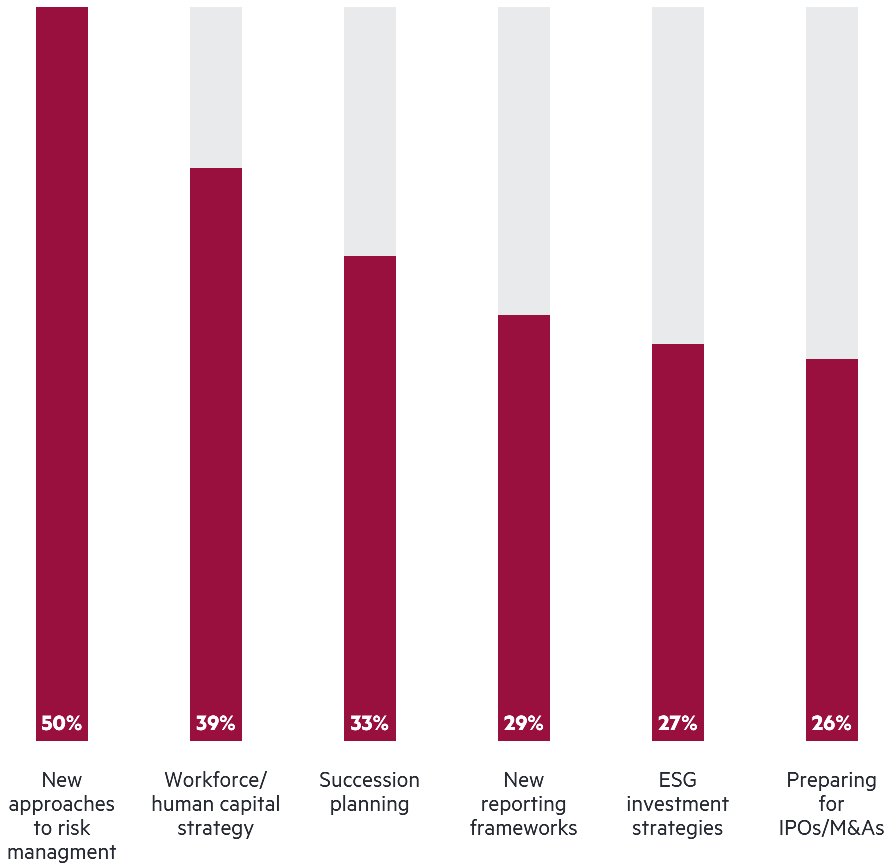
Sam Mostyn agrees that being a board member has become more complex. "You have to know why you want to be a director in order to take on both that duty and that risk," she says. "High-performing boards represent a mix of people and skills that are capable of managing the complexity of their industry and the business they are governing."

Elkington says that getting this knowledge balance right comes back to how organisations recruit their board members. If they are allowed to flourish, newer board members can make valuable early contributions to the strategic and cultural direction of companies.

"People who join boards often assume that they have to be seen to conform to existing assumptions and systems," he says. "But one of the things that is really valuable to boards is to access contrary and alternative perspectives. To get an early feel for different future trajectories. So, even if you do not go there immediately, the fact that you can test your plans, your strategies and your mindsets against different perceptions of reality is hugely valuable."

WHERE DIRECTORS WOULD WELCOME MORE GUIDANCE

On which of the following board issues would you personally most welcome more insight and guidance?



Why networks work

To offer a nuanced perspective on board matters and decisions, directors need to stay up to date on issues related to strategy, risk, remuneration, ESG, diversity and inclusion.

Respondents say that reports and intelligence from senior leadership, as well as market intelligence, are most valuable in helping them to carry out their board responsibilities (see graphic).

A board's access to a range of data sources – and their ability to analyse it effectively – is becoming critical. It is one of the reasons why the IoD in the UK created a data governance learning programme with the Open Data Institute.[22]

Previous FT research has found that a number of organisations report significant gaps in the intelligence that they are able to secure. As a result, their ability to scan the horizon is curtailed.[23]

One way for directors to take a lateral approach to decision-making is to broaden not only their data sources, but also their range of influences. More than a third of directors (36%) say that peer-to-peer networks are valuable. Nayantara Bali says that the Singapore Institute of Directors, which offers regular seminars from experts, helps build the capability and understanding of directors.

She also explains why informal networking is critical to directorial development.

"I am very active in my alumni network," she says. "There is lots of young talent in start-ups and new roles, and I hear what is going on and the issues that people are talking about — what is senior management struggling with?"

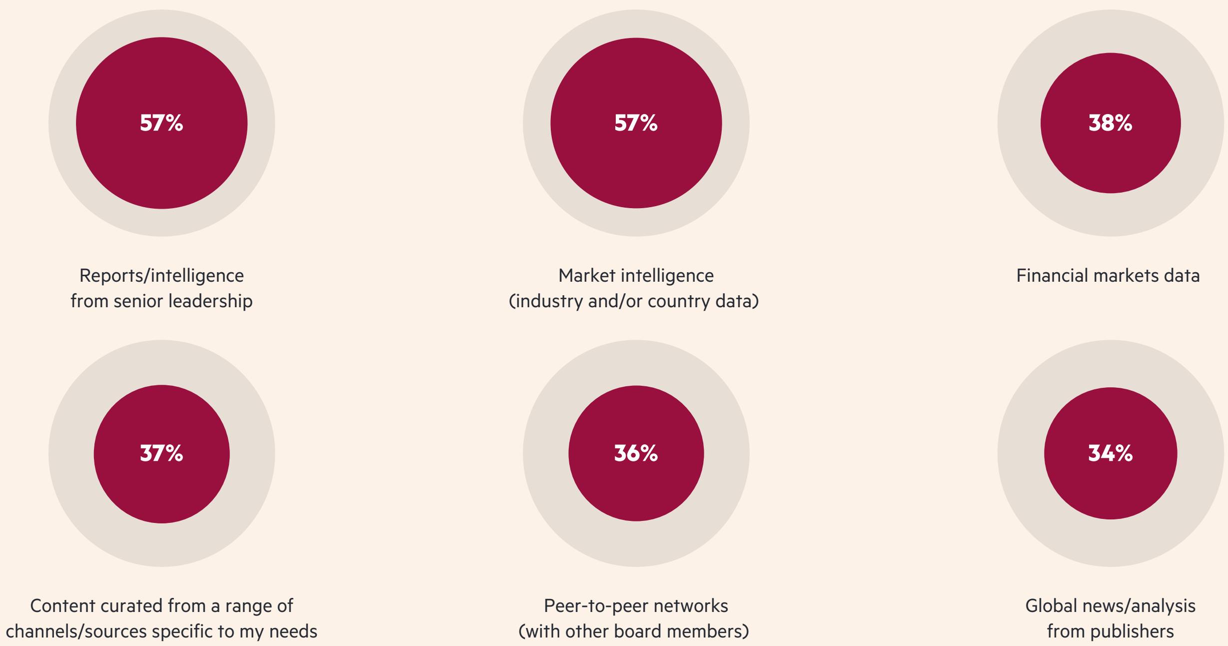
Neglect this kind of peer-to-peer communication, and directors risk losing touch with the commercial and cultural context of leadership issues – and the opportunity to debate and exchange ideas with fellow board members.

"Directorship is becoming a profession," says Ruth Medd. "It is becoming a community, so your challenge is to build up your knowledge and your contacts. There are things that you should do each year; you need to understand changes in directors' duties, in financial statements, in risk management. There is no substitute for professional development."

> "Directorship is becoming a profession. It is becoming a community, so your challenge is to build up your knowledge and your contacts.
>
> RUTH MEDD,
> CHAIR OF WOMEN ON BOARDS

SOURCES OF SUPPORT

How valuable are each of the following in helping you fulfil your board responsibilities?



Percentages show net scores of 8, 9 and 10 on a 10-point scale, where 0 is not at all valuable and 10 is extremely valuable

CONCLUSION:

BUILDING BETTER BOARDS

The way that board directors think, operate and collaborate is changing. Their remit is growing, but so is interest in the art and science of directorship. As boards continue to evolve at pace, there are a number of focus areas for directors and senior leaders to consider.

Update your intelligence
For John Elkington, the ongoing aim for boards must be to stay engaged and relevant. “If the board is not properly addressing the agenda that senior executives are already experiencing, the latter will start to bypass them,” he says. Directors need to absorb a range of expert insights and perspectives — and understand the impact of economic and geopolitical trends. Board members need to ask more of themselves, as Sam Mostyn explains: “There is a greater onus on directors to be more skilled in much broader areas than before.”

Seek diversity of perspective and personality
There are signs that corporates are addressing gender inequality on boards, but the problem runs much deeper. Companies need to think more carefully about the breadth of professional and personal experience that the board can draw upon. Do they have the right mix of skills to manage the complexity of the business and sector in which they operate? They then need to assess the structure, frequency and dynamics of meetings to ensure that all voices are heard.

Embrace change
The next 10 years, says Elkington, are likely to be an “exponential decade” for business in terms of change. And this will either be “exciting” or “deadly” — depending on how organisations approach the shifting landscape. “The board is central to change on this scale,” he says. “Get it right, and you potentially get everything right.”

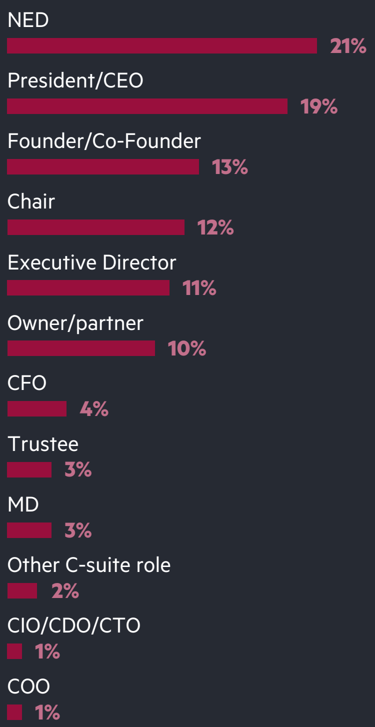
Rethink recruitment
For too long, board directors were recruited from a narrow list of known candidates. Beyond the traditional search firms, there is a growing sophistication in how director roles are scoped in terms of skills, responsibilities and expectations. Greater transparency on appointments will help raise the bar on boardroom recruitment.

Grow your networks
With the role of the board director changing at pace, peers provide a much-needed sounding board. Just as companies should extend the reach of their recruitment of directors, so board members should seek a wide range of expert input to update their knowledge and freshen their perspective. Training and development opportunities abound. Now is the time to extend your network and consider joining communities of fellow directors.

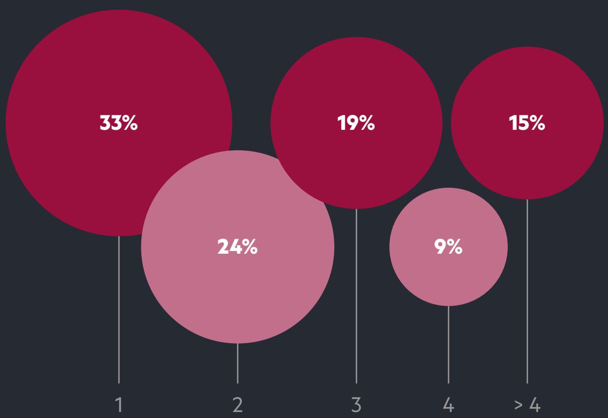
ABOUT THE RESEARCH

The data in this report is based on a survey of 626 respondents conducted in March 2021. All respondents currently sit on the board of at least one company.

ROLE



TOTAL OF BOARD POSITIONS CURRENTLY HELD



PRIMARY LOCATION

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