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# NOMINATING/GOVERNANCE COMMITTEE:

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## OVERSIGHT OF BOARD COMPOSITION, FUNCTION & EVALUATIONS

# Recruitment & Nomination

**A core responsibility of the nominating/governance committee is the oversight of the composition of the board and its committees. Board and committee composition lie at the heart of board effectiveness. The ideal board comprises a diverse group of directors from widely varying backgrounds offering complementary expertise who work well as a team and who possess the skills necessary for board and committee work. The ability to recruit the right directors and integrate them successfully is one of the clearest indicators of a high-functioning board.**

## **BOARD COMPOSITION: A STRATEGIC ASSET**

Boards ideally view their composition as a strategic asset, annually reviewing their makeup in light of company strategies and competencies that would be valuable to have in future boardrooms. Nominating/governance committees generally consider a variety of variables when recruiting new directors and determining whether to recommend the nomination of sitting directors.

Some nominating/governance committees use a board skills matrix to examine the demographics and professional backgrounds of current board members and evaluate the board's composition. Some boards are disclosing a skills matrix in publicly available materials such as the proxy statement. See Section 1 for a sample skills matrix recommended by the New York City comptroller and the New York City pension funds.

## **DEVELOPING A SKILLS MATRIX**



Identify the key skills, backgrounds and experience necessary to oversee forward-looking strategies and risks, while satisfying legal requirements and committee needs.



Inventory the skills, contributions and diversity of current board members.



Identify gaps in skills, backgrounds and experiences to shape searches and influence decisions to renominate directors.

## S&P 500 NEW DIRECTOR BACKGROUNDS

**50%**



of new directors are women or minorities

**428**



new independent directors

**33%**



of new directors are serving on their first public board

**34%**



of new independent directors have backgrounds in the technology or telecommunications industry

Source: 2018 U.S. Spencer Stuart Board Index

## BUSINESS STRATEGY

Strategy is the starting point for every review of board composition. The sheer pace of change means that companies—and boards—are having to respond to market, competitive, technology, political, regulatory and customer changes that are coming at them faster than ever.

The nominating/governance committee is the front line for ensuring that the board is composed of directors with the right skills and qualifications to oversee forward-looking strategies and emerging threats and opportunities. Each year, the nominating/governance committee should consider the company's strategy for the next several years, assess whether the current board composition aligns with company strategies and plan to address any gaps.

A balanced board will be comprised of directors who bring specific experiences, skills and perspectives and yet who are also capable of contributing to board decisions on topics that may fall outside their sphere of expertise. In other words, they need to have sufficient financial and business acumen that they will not be left behind in any aspect of board debate.

Boards look to the nominating/governance committee to determine the specific backgrounds, expertise and experience that are relevant for the board as a whole and its individual members relative to company strategies. Based on strategic considerations, some boards are identifying new boardroom needs and prioritizing new areas of expertise. They are tapping "nontraditional" candidates, especially younger, active executives, to bolster their knowledge in disciplines such as digital or social media, e-commerce, certain areas of finance and emerging markets or global business. Nominating/governance committees are also considering directors without previous board experience.

# Requirements & Considerations

## INDEPENDENCE REQUIREMENTS

The nominating/governance committee is responsible for reviewing the independence of directors and board committees to ensure compliance with stock exchange requirements.

## LISTING REQUIREMENTS

### New York Stock Exchange

Independent directors must comprise a majority of the board.

Boards must have all-independent audit, compensation and nominating/governance committees (with limited exceptions).

### NASDAQ Stock Market

Independent director must comprise a majority of the board.

Boards must have all-independent audit and compensation committees.

Boards must have an all-independent nominating/governance committee or nominees must be selected by independent directors constituting a majority of the board's independent directors (with limited exceptions, including: under certain limited circumstances and with additional disclosures, one non-independent director may serve on the audit, compensation or nominating/governance committee for no longer than two years).

Both exchanges have specific minimum definitions for determining director independence and also require boards to affirmatively determine that directors who are classified as independent have no material relationship with the company, either directly or as a partner, shareholder or officer of an organization that has a relationship with the company.

For more details on independence: [NASDAQ definition](#) [NYSE, 303A.01 and 303A.02](#)

Institutional investor proxy voting guidelines may incorporate more stringent standards for director independence. As a result, nominating/governance committees should consider whether directors satisfying exchange independence standards run afoul of investor standards for independence.

Some investors have questioned whether directors with "excessive" tenure should still be considered independent, and a few consider tenure when assessing director independence. While tenure is a director independence consideration in some markets outside of the U.S., there are currently no specific regulations or listing standards in the U.S. that link director independence to tenure.

## COMMITTEE NEEDS

Nominating/governance committees must also consider committee needs, including regulatory requirements, legal considerations and policies—such as rotation—related to board committee leadership and membership. Knowledgeable, independent directors are needed to lead and serve as members of the audit, compensation, governance and other committees. The chair, especially, must be current on the relevant governance issues and trends related to each committee.

The majority of boards maintain between three and four standing committees.

## PREVALENCE AND INDEPENDENCE OF STANDING COMMITTEES AMONG S&P 500 COMPANIES

	% with this committee		% composed entirely of independent directors	
	2018	2013	2018	2013
Audit	100%	100%	100%	100%
Compensation	99.8%	100%	99.6%	99.6%
Nominating/Governance	99.4%	99.4%	99.6%	100%
Executive	30%	36%	2%	2%
Finance**	31%	31%	76%	78%
Risk	12%	8%	77%	72%
Science & Technology	9%	10.5%	93%	88.5%
Public Policy/Social & Corporate Responsibility	9%	8%	87%	74%
Environment, Health & Safety	9%	8%	84%	90%
Legal/Compliance	4.5%	5.5%	86%	90%
Strategy & Planning	2%	4%	50%	72%
Investment/Pension	3%	3%	59%	77%

\*12 boards have a combined compensation and nominating committee. They are counted as separate committees for the purpose of this analysis.

\*\*Includes two boards with a standing corporate governance committee in addition to the nominating committee. Controlled companies are not required to have nominating committees.

\*\*\*13 boards have a combined finance and risk management committee. They are counted as separate committees for the purpose of this analysis.

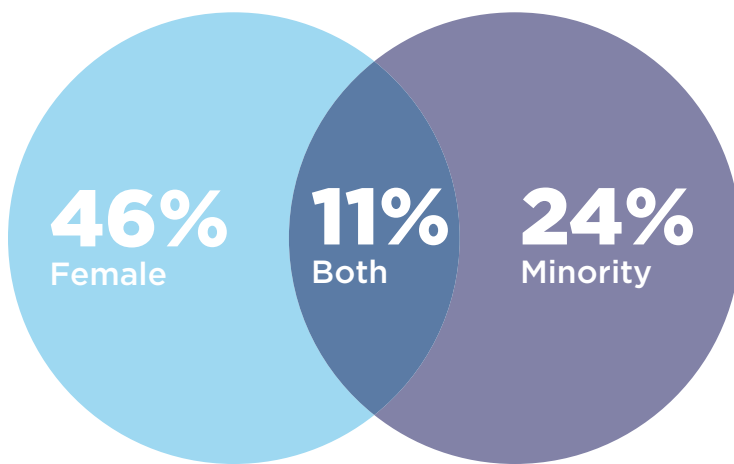
Source: 2018 U.S. Spencer Stuart Board Index

# Diversity

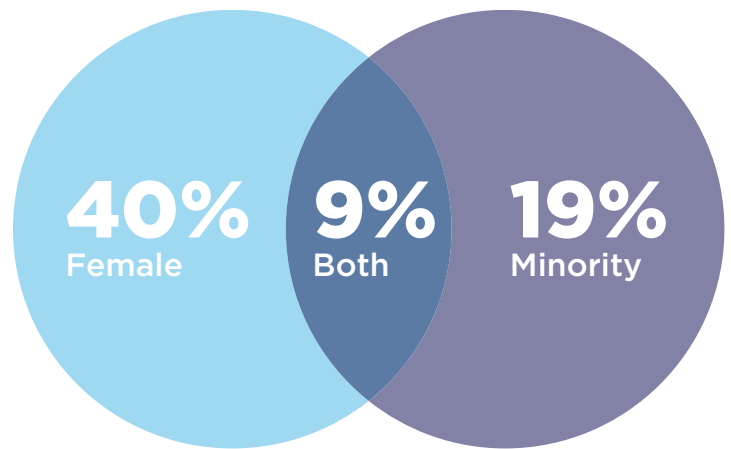
Boards increasingly appreciate the value of having diverse perspectives—in the areas of age, gender, race and ethnicity and, in some cases, geographic knowledge—to foster better debate and decision-making and less groupthink. Diversity takes many forms, and the relevant mix of perspectives sought by a board will vary depending on factors such as the scale of the business and demographic considerations such as customer base and geographic footprint.

## BOARDS ARE TAKING STEPS TO ENHANCE BOARDROOM DIVERSITY

First-Time Directors (% S&P 500)



All New Directors (% S&P 500)



Source: 2018 U.S. Spencer Stuart Board Index

## GENDER DIVERSITY

In recent years, female representation on boards in particular has been a growing area of focus, with a variety of stakeholders criticizing the slow pace of progress. Boards face more pressure on gender diversity from institutional investors, who point to research showing that companies with more diverse boards—and, especially, more women—perform better.

## RACIAL AND ETHNIC DIVERSITY

Increasing ethnic and racial diversity is another priority for many boards. According to Spencer Stuart's 2018 survey of nominating/governance committee members, 43 percent indicated that recruiting minority directors was a priority.

## INTERNATIONAL DIRECTORS

Another consideration is whether to add an international perspective to the board. For example, it may be valuable to have one or more directors from strategic markets or with working experience in those markets if the company is expanding its global footprint, building manufacturing or distribution capabilities overseas or moving into a complex or particularly competitive market. A number of dimensions should be considered when thinking about adding international representation to the board, including differing time zones, languages, customs and cultural nuances. International directors remain a small minority on U.S. boards, accounting for just 8.2 percent of directors in the top 200 S&P 500 companies. By comparison, boards in eight European countries average more than 30 percent foreign directors, with foreign directors representing 58 percent of directors of Swiss boards.

Boards do not have to sacrifice critical skills or expertise to increase diversity, but they may have to broaden their approach to director recruitment and their perceptions about the ideal director. For example, boards often define the ideal board member as a current or former CEO or CFO, and women and minorities are still underrepresented in these ranks.



# Onboarding New Directors

Onboarding programs are designed to familiarize new directors with the company's businesses, strategies and policies and to assist new directors in developing the skills and knowledge required for board service. While many boards do not explicitly place responsibility for new director onboarding with the nominating/governance committee, on many boards the committee plays a supporting role with the corporate secretary and board chair.

A thorough, tailored program should bring the director up to speed on key topics, ranging from the board's structure, governance and responsibilities to the company's strategic objectives, financial reporting and relationships with investors and management.

If a new board member has prior director experience, the onboarding program can focus on the company, its products, services and key players; the wider business context; and the culture of the board and how it operates. A first-time director without previous board experience will also benefit from general training on the role of the board and individual directors, important governance regulations and listing requirements and the governance issues affecting boardrooms today. And in all cases, new directors should also own the onboarding experience by taking responsibility for ensuring they are getting the training and insights needed to quickly get up to speed in the boardroom.





## DIRECTOR ONBOARDING BEST PRACTICE PROCESS



Meetings with key business executives and functional leaders, including finance, marketing, IT, HR, legal, internal audit

- Presentations on the business model, key performance indicators (KPIs), profitability and performance
- Explanation of regulatory and governance issues
- Overview of the operations, operational challenges and underlying infrastructure
- Overview of the company's risk profile, including how the board views sector and company risk and how management assesses, presents and articulates risk
- Overview of board calendar activities—not just what the next board meeting is about but the key processes of the board over the course of 12 months of board meetings
- Discussion of director roles and responsibilities (key for first-time directors)



Meet one-on-one with as many directors as possible to provide a sense of the priorities of the board and the dynamics among directors and between management and the board



Review prior 12 months' board materials and minutes to provide context on the current issues



Visit operations to get a better sense of how the business works and an opportunity to meet people on the ground



Meet with external advisers such as accountants, bankers, brokers and others



Attend investor day



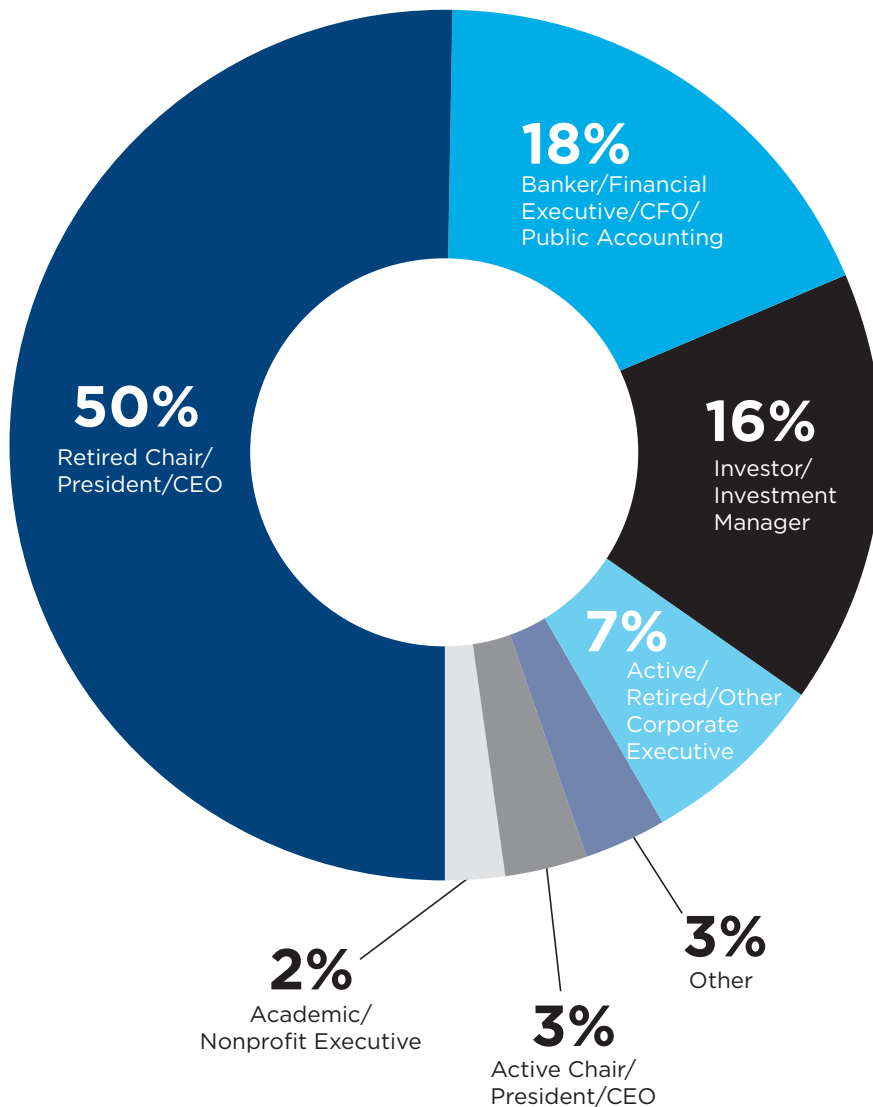
Assign a mentor (*Note: First-time directors especially tell us they appreciate having a mentor during the first six to 12 months on the board. An informal mentor program pairs a new director with a more experienced director who can provide perspective on boardroom activities and dynamics or help with meeting preparation, explain aspects of board papers and debrief and act as a sounding board between meetings.*)

# Board Leadership

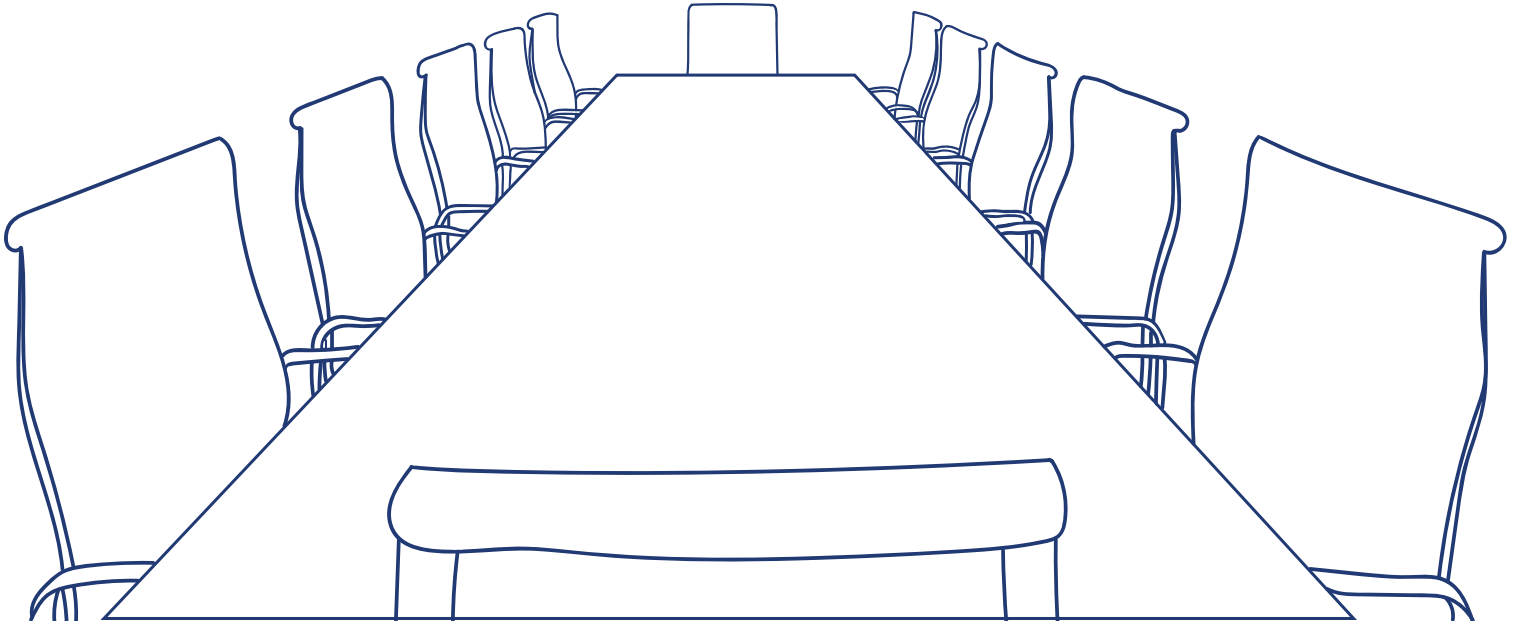
Nominating/governance committees generally are responsible for recommending the board's leadership structure. Investors expect boards to have robust independent board leadership, and some advocate independent chairs as the best structure. Today, S&P 500 boards are more likely than in the past to split the chair and CEO roles between two people. However, independent chairs—a director who meets the applicable NYSE or NASDAQ rules for independence—are less common; only 30.5% of S&P 500 boards, versus 28% in 2017 and 16% in 2008, have an independent chair. Among the 92 boards where the chair is separate but not independent, nearly all (93.5%) have identified a lead or presiding independent director.

Half of S&P 500 independent chairs are retired senior executives.

## INDEPENDENT CHAIR BACKGROUNDS AMONG S&P 500 COMPANIES



Source: 2018 U.S. Spencer Stuart Board Index



## QUESTIONS YOU SHOULD ASK: BOARD COMPOSITION

1

Does the board as currently constituted give the company its best shot at success in supporting the strategy?

2

Would additional, and perhaps different, skills significantly enhance the board's ability to do its job?

3

How do stakeholders, including investors, view the diversity of the board and its leadership?

4

Does the nominating/governance committee routinely look ahead to identify boardroom needs and anticipated turnover?

5

What is the refreshment strategy and how is it communicated to stakeholders, including investors?

6

What is the composition of director tenure and how does it benchmark against peers and investor expectations?

7

Is there a mix of tenures in the boardroom?

8

Is our onboarding program robust and tailored to individual needs and backgrounds?

# Spotlight on Board Composition

**Institutional investors increasingly are scrutinizing board composition.**

**“We view the board as one of a company’s most critical strategic assets. When the board contributes the right mix of skill, expertise, thought, tenure and personal characteristics, sustainable economic value becomes much easier to achieve. A thoughtfully composed, diverse board more objectively oversees how management navigates challenges and opportunities critical to shareholders’ interests. And a company’s strategic needs for the future inform effectively planned evolution of the board.”**

*August 31, 2017, An open letter to directors of public companies worldwide, F. William McNabb, III, Chairman and CEO, Vanguard*

**“Our primary concern is that board members are able to contribute effectively as corporate strategy evolves and business conditions change, and that all directors, regardless of tenure, demonstrate appropriate responsiveness to shareholders. We acknowledge that no single person can be expected to bring all relevant skill sets to a board; at the same time, we generally do not believe it is necessary or appropriate to have any particular director on the board solely by virtue of a singular background or specific area of expertise.”**

*2018 Proxy Voting Guidelines for U.S. Securities, BlackRock*

## TURNOVER

Turnover on U.S. boards has largely been driven by director retirements. Other forces—including activist investors, mergers and acquisitions or the emergence of a need for new perspectives and skills on the board (such as financial expertise after the passage of the Sarbanes-Oxley Act of 2002 and, more recently, digital and cybersecurity experience or diversity (also influence board composition).

The vast majority of board departures are known about well in advance, giving the nominating/governance committee time to engage in boardroom succession planning and to carefully consider the desired profile and expertise of successors.

As a starting point, the nominating/governance committee should stay up to date on the timing of anticipated vacancies, including those due to term or age limits and director plans for retirement. Today, most nominating/governance committees start planning for vacancies at least 12 months in advance and, in cases when several retirements are on the horizon, governance committees think holistically about a multiyear process.

U.S. boards today rely overwhelmingly on formal retirement policies to promote turnover. Among S&P 500 companies, for example, 71 percent report having a mandatory retirement age for directors.

## S&P 500 BOARD RETIREMENT AGES

	2018	2013	2008
70 and younger	3%	11%	27%
71	1%	1%	1%
72	43%	55%	55%
73	4%	4%	4%
74	6%	5%	2%
75 and older	43.5%	24%	11%

Source: 2018 U.S. Spencer Stuart Board Index

Mandatory tenure policies are less common. Only 5 percent of S&P 500 companies set explicit term limits, with a majority of the policies set at 15 years or more. Nearly two-thirds (65 percent) of S&P 500 boards explicitly state in their corporate governance guidelines that they do not have term limits.

Increasingly, meaningful assessments are viewed by investors as the preferred tool for evaluating and enhancing board and director performance and promoting boardroom refreshment. They consider peer and/or self-assessments best practices for providing feedback to directors on their performance, identifying gaps in boardroom skills and perspectives, and facilitating boardroom succession. Despite investor support, individual director evaluations are not prevalent. The 2018 U.S. Spencer Stuart Board Index found that only 38% of S&P 500 companies reported some form of individual director assessments in their process—a percentage largely unchanged over the previous five years.

Some boards are emphasizing that directors should not expect to be renominated annually and that the board self-evaluation process is an important determinant for board tenure. Boards taking this approach use annual evaluations to assess the effectiveness of the board overall as well as the contributions of individual directors to identify directors who are underperforming or whose skills no longer represent a good fit with the strategic direction of the business.

# Corporate Governance Principles

**While director and board effectiveness and performance are ultimately the responsibility of the full board, the nominating/governance committee plays a critical role with its oversight of the board's governance policies and practices, governing documents, committee structures and annual evaluations. The nominating/governance committee is also often responsible for overseeing the required code of ethics and conduct for directors, officers and employees.**

## CORPORATE GOVERNANCE PRINCIPLES

Companies listed on the NYSE are required to adopt and publish corporate governance guidelines summarizing their governance philosophies and practices. NASDAQ-listed companies aren't required to have formal corporate governance guidelines. However, they are generally considered best practice, and today most boards have adopted governance guidelines.

**The following subjects must be addressed in the corporate governance guidelines required by the NYSE:**

1

### Director Qualifications Standards

These standards should, at minimum, reflect the independence requirements set forth in the NYSE Listed Company Manual. Companies may also address other substantive qualification requirements, including policies limiting the number of boards on which a director may sit, director tenure, retirement and succession.

2

### Director Responsibilities

These responsibilities should clearly articulate what is expected from a director, including basic duties and responsibilities with respect to attendance at board meetings and advance review of meeting materials.

3

### Director Access to Management and, as Necessary and Appropriate, Independent Advisers

4

### Director Compensation

Director compensation guidelines should include general principles for determining the form and amount of director compensation (and for reviewing those principles, as appropriate). The board should be aware that questions as to directors' independence may be raised when directors' fees and emoluments exceed what is customary. Similar concerns may be raised when the listed company makes substantial charitable contributions to organizations in which a director is affiliated or enters into consulting contracts with (or provides other indirect forms of compensation to) a director. The board should critically evaluate each of these matters when determining the form and amount of director compensation and the independence of a director.

# 5

## Director Orientation and Continuing Education

# 6

## Management Succession

Succession planning should include policies and principles for CEO selection and performance review, as well as policies regarding succession in the event of an emergency or the retirement of the CEO.

# 7

## Annual Performance Evaluations of the Board

The board should conduct a self-evaluation at least annually to determine whether it and its committees are functioning effectively.

# 8

## Requirements

**Website Posting Requirement:** A listed company must make its corporate governance guidelines available on or through its website.

**Disclosure Requirements:** A listed company must disclose in its annual proxy statement or, if it does not file an annual proxy statement, in its annual report on Form 10-K filed with the SEC that its corporate governance guidelines are available on or through its website and provide the website address.

# Continuing Education

Expectations of corporate boards and directors have never been higher. They are expected to be more engaged, more knowledgeable and more effective than in the past. At the same time, business disruptors and risks are evolving at an unparalleled pace, and the roles and responsibilities of directors are growing increasingly complex. Director education is considered a best practice for establishing a boardroom culture of continuous improvement and for positioning individual directors and boards for success in today's ever-changing business environment.

Directors do not have to be licensed, certified or otherwise satisfy minimum standards to serve on corporate boards, and companies are not required to provide directors with training or continuing education. However, today's companies and investors generally expect that corporate directors will be committed to optimizing their performance by participating in training and continuing education on current and emerging issues and rules and regulations relevant to the boardroom.

Companies may offer a variety of educational programs and opportunities to help directors best perform their duties and stay abreast of emerging issues.

## BOARDROOM APPROACHES TO DIRECTOR CONTINUING EDUCATION

- Hosting regularly scheduled, in-boardroom educational sessions featuring internal and external experts on topics of particular relevance to the company and its business
- Paying reasonable expenses related to third-party educational programming related to director responsibilities
- Providing directors with an educational budget to be used, as they elect, for boardroom related training and education
- Covering membership dues for board-focused organizations
- Encouraging participation in free educational programming available to directors, including webinars and events sponsored by professional firms, such as law and accounting firms





Companies are not required to disclose details about director training and ongoing education. However, NYSE-listed companies must address director education and orientation in their corporate governance guidelines.

To help spread knowledge gained through continuing education, boards may allocate a few minutes of each board meeting for directors to share takeaways from recent educational programming, or they may designate a location (such as the portal for board materials) for directors to share information or summarize learning.

## QUESTIONS YOU SHOULD ASK: COMMITTEE OVERSIGHT FUNCTIONS

1

Are our governance policies and documents (bylaws, charter) current and best structured for the unique considerations of the board and the company?

2

How do our corporate governance policies and key provisions of our governing documents benchmark against peers and investor expectations?

3

What feedback, if any, have we received from investors and other stakeholders about our governance policies and documents?

4

Does the board have a commitment to supporting continuing education for directors?

5

What mechanisms are in place to encourage sharing of learning from director continuing education programs?

# Evaluations: Board

Nominating/governance committees generally take the lead overseeing annual board evaluations, which boards are increasingly using to examine and improve their effectiveness. Annual assessments have become the norm for boards in many countries, with nearly all listed companies in Canada, France, the UK and the U.S. conducting some sort of assessment each year. Annual evaluations are also widespread in Italy and Spain and gaining attention in many Asia Pacific markets, where the issue of board effectiveness is moving up on the corporate governance agenda.

Done effectively, board evaluations provide a forum for directors to review and reinforce appropriate board and management roles, highlight best practices and ensure that problem areas or gaps are identified and addressed promptly.

Since board structures, governance issues and cultural norms differ by company and country, one size does not fit all when it comes to board assessments. To be most effective, a board assessment must be tailored to a company's current business context and unique circumstances.

An independent facilitator may be engaged by the board to assist with the annual evaluation. In some markets, boards are required to engage a third party to facilitate board evaluations. Many boards hire third-party facilitators periodically (such as every third year) or as needed in response to changing board dynamics or emerging challenges.

## IN OUR EXPERIENCE, BOARDS DERIVE THE HIGHEST VALUE FROM A BOARD ASSESSMENT SHAPED BY FIVE KEY PRINCIPLES:



### **The Board Agrees on Clear Objectives for the Assessment**

A shared agreement among directors about the goals for the assessment encourages directors to commit to the process and provide the candid feedback essential to identifying and addressing potential roadblocks to board effectiveness.

For some boards, a “triggering event,” such as the arrival of a new CEO or a change in board leadership or composition, can shape the priorities and objectives of the assessment. For example, an assessment occurring during a CEO transition can help forge an understanding between the CEO and the board about expectations and accountabilities, clarify the respective roles of the board and CEO and ensure that time is spent early in the CEO's tenure to consider whether changes are needed in the way the board is composed, structured or operates.



### **A Board Leader is Responsible for Driving the Process**

Essential to a successful evaluation is having an independent board leader champion the assessment process. The independent board chair, chair of the nominating/governance committee or the lead independent director is in a position to drive the process and involve the right people, ask for directors' time, schedule time on the agenda to discuss the results and ensure that the board follows up on the issues that emerge. While the CEO should be an integral part of the process, he or she should not be leading it.

The board leader driving the assessment process plays a significant role in managing expectations about the process, serves as an independent resource for directors and management to turn to with concerns and may deliver feedback to individual directors, if the board is not working with a third party to facilitate the process.



### **The Process Incorporates Perspectives Beyond those of Directors, Including those from Senior Management and Best Practices from Outside the Company**

One way the board can limit the value of a board assessment is to look only inwardly at its own effectiveness. An emerging best practice among U.S. boards, although still less common in European boards, is to seek input from the key senior management team members who interface with the board. Soliciting input from the executives who participate in most of the board meetings—such as the general counsel, the president, the chief financial officer and head of human resources—can broaden the perspectives on the board’s effectiveness in key areas, including board/management relations. As regular board observers, these executives often have very thoughtful feedback about what the board does well and what it could do better.

Board assessments also can be more valuable when boards benchmark themselves against other high-performing boards in the same industry segment or against best practices in specific areas. For example, boards often want to know how they compare to peers in areas such as committee structure, compensation and mandatory retirement age. A third-party facilitator with significant experience in the boardroom and knowledge of governance guidelines and regulations can provide perspectives on how the board compares to its peers or measures up to the evolving standards of corporate governance by providing an up-to-date perspective on best practices.



### **The Assessment Process Goes Beyond Compliance Issues to Examine Board Effectiveness**

Done well, the assessment process can reveal a variety of issues and obstacles to high-performing boardrooms. These range from easily addressed operational complaints about meeting length or the composition of the agenda, to larger, thornier issues concerning the board’s role in strategic decision making, gaps in knowledge and competencies on the board, and executive and director succession planning. Corrective actions range as well—from improving the timeliness of board materials and winnowing overly long agendas to making changes in the composition and, occasionally, the leadership of the board.

While many of the concerns that surface through evaluations focus on board procedures, they sometimes go to the important relationship between the board and management, which can vary depending on the size and development stage of the company, the international makeup of the board and the current state of the business. In Europe, many boards also are re-examining the board’s involvement in areas such as succession planning and strategy planning, considering whether the board should be more involved earlier in the process, for example, to review the competitive assumptions shaping management’s strategic plan.



### **Directors Commit to Reviewing the Results of the Assessment and Preparing an Action Plan for Addressing Issues that Emerged**

Assessments can fall short when boards do not commit the time to review the results and address the issues that are raised. Some boards, for compliance reasons, begin an assessment process, but then spend little or no time discussing the findings. In addition to leaving issues unresolved, this lack of follow-up can generate cynicism about the process and the board leadership’s commitment to improving effectiveness in the future.

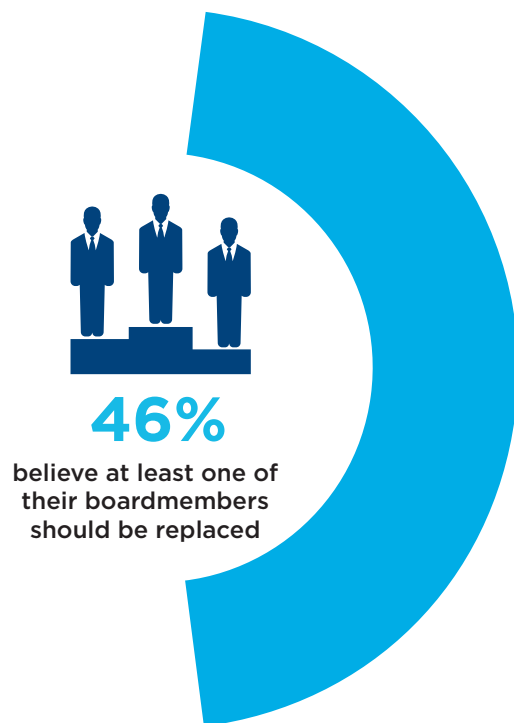
Boards have to be open to the results of the assessment and committed to dealing with the findings. This involves having an open discussion among the board members about performance issues that were raised and prioritizing items that should be addressed in the coming year. Follow-up is typically delegated to the nominating/governance committee, which develops an action plan based on the board’s recommendations. The board reviews its progress as part of the following year’s assessment.

# Evaluations: Individual Director

Annual board evaluations are increasingly standard practice in boardrooms around the globe. And increasingly boards are retaining independent experts to assist with evaluations.

Individual director assessments—whether self or peer—appear to be less common. The 2017 Spencer Stuart U.S. Board Index found that just over one-third (37%) of S&P 500 companies disclose some form of individual director assessments in their process—a percentage largely unchanged from five years ago.

Despite the challenges, consensus is growing in support of conducting individual director assessments as part of the board effectiveness assessment—not to grade directors but to provide constructive feedback that can improve performance. High-performing boards expect directors to stay engaged and to contribute fully and are willing to address underperformance. They also create an environment that encourages individual directors to think critically about their contributions and the relevance of their skills to the company strategy.



Source: PwC, 2017 Annual Corporate Directors Survey



The need for mechanisms, such as assessments, for providing feedback to directors is evident. PwC surveys have consistently found that significant percentages of directors believe one or more colleagues on the board should be replaced, citing reasons such as directors overstepping the boundaries of their oversight role, failing to challenge management or interacting in ways that negatively affects board dynamics. Advanced age and diminished performance are also cited.

The collegial nature of the boardroom, so vital to board effectiveness, can make peer assessments uncomfortable for directors. Because it can be difficult to share negative feedback about a fellow director, peer assessments may be avoided or can become compliance exercises that fail to address any elephants in the room.

Some boards use a formal individual director assessment or a peer assessment process. Others may implement a mentoring program for directors. Another approach is have each director meet periodically with the chairman/lead director or nominating/governance committee chair.

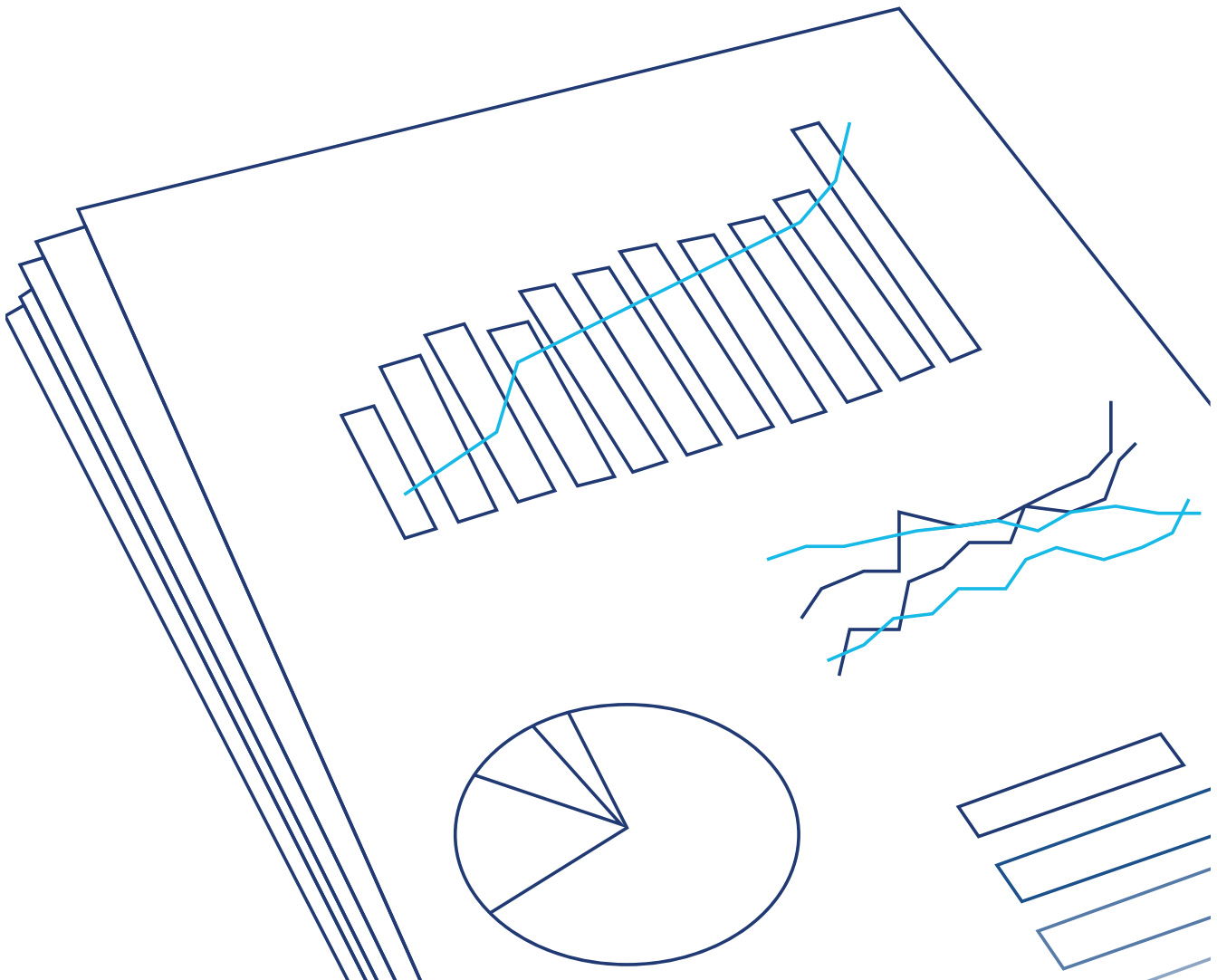
Board leadership plays a critical role in ensuring directors receive important feedback, since they frequently receive feedback on individual directors or observe behavior in meetings that can be improved. High-performing board chairs and lead directors will embrace this role.

# Evaluations: Disclosure & Engagement

Shareholders are seeking more information about how boards address their own performance, including whether they are using assessments as a catalyst for refreshing the board. Disclosures are currently fairly limited in this area. Beyond reporting that boards conduct an annual assessment, most S&P 500 boards disclose few details about their assessment process. However, companies are starting to offer more detailed disclosures, including descriptions of the areas that the board assessment covers, the process and the actions the board has agreed to take following the assessment.

Today, large institutional investors such as BlackRock, State Street and Vanguard are calling for greater transparency about how candidly boards are addressing their own performance and the suitability of individual directors. The Council of Institutional Investors (CII) suggests that enhanced disclosure “is an indication that a board is willing to think critically about its own performance on a regular basis and tackle any weaknesses.”

CII highlights two best-practice models for disclosure. One focuses on the mechanics of the assessment process, illustrating the process the board uses to identify and address gaps in its skills and performance. The other focuses on the most recent assessment, recapping the key takeaways and plans for improvement.



## QUESTIONS YOU SHOULD ASK: BOARD EVALUATIONS

1

What is the scope of the assessment?

- Board
  - Board committees
  - Individual directors
- Board leaders (independent chair, lead director, presiding director, committee chairs)

2

What is the most appropriate assessment approach for the board?

- Director questionnaire
- Director interviews

3

Who should lead the assessment?

- Third-party facilitator
- Independent chair, lead director and/or nominating/governance committee chair

4

What gaps exist in the current assessment process?

5

What will be publicly disclosed about the board evaluation?

6

What is the process for discussing the results of the evaluation and developing an action plan to address key areas?

7

Who is responsible for ensuring follow-up on evaluation takeaways?

8

What areas does the board want to delve into more deeply?

- Board processes
- Agendas and materials
- Board behaviors and dynamics
- Communication issues
- Effectiveness of executive sessions
- Role of the lead independent director
- Board relationship with the CEO and management
  - Board composition
- Committee organization and processes
- The role of the board and board leaders
  - Board culture and dynamics
- Potential board development needs
  - Overall board effectiveness
  - Individual effectiveness

*Note: in countries where annual assessments are required, some boards find the process more valuable when they choose a specific topic each year—such as the board's committee structure or its role in the strategic planning process—to examine more closely.*

# For More Information

This paper is an excerpt from the Nominating/Governance Committee Fundamentals Guide, a comprehensive guidebook created for Corporate Board Member's Board Leadership Program with content provided by Spencer Stuart's North American Board Practice.

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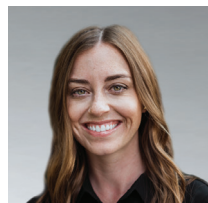
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