



WHITE PAPER

Smart Diversity: Board Composition as a Competitive Advantage

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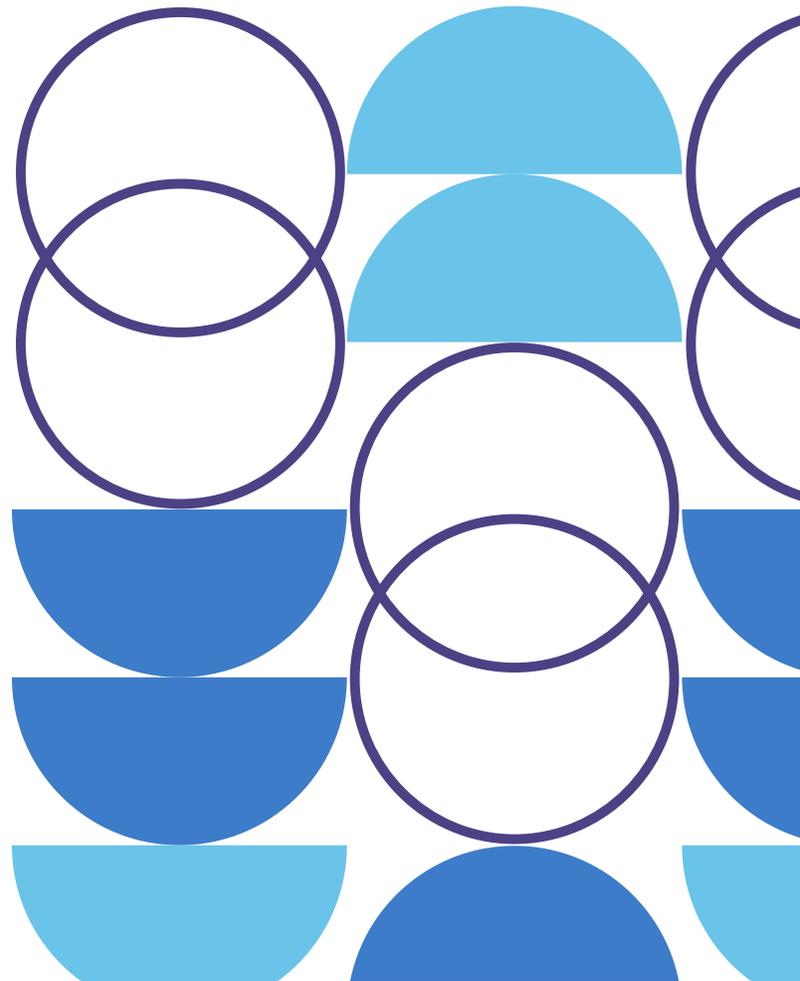


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Preface

In this White Paper, we will investigate the motives driving increased scrutiny of board composition in today's world. We will then explore strategies for creating a more effective board composition that can build synergies and create value in the board room. Finally, we will talk about harnessing technology to increase board effectiveness.



Understanding Why Board Composition Matters

A quick introduction to board composition and today's research

You have all heard the recent call for a more diverse board, but do you really understand what that means and how to get there? As consumers and workers have become more diverse, the boardroom's basic demographics have stayed resolutely uniform. These circumstances have set into motion research on the impact of board composition. That research has found:

- Directors are growing increasingly dissatisfied with at least one member of their board
- The most cited reasons for this growing dissatisfaction are age and unpreparedness
- A high level of board diversity (women, minorities, and expertise) has been found to be correlated to overall enterprise profit levels

"Directors know their boards need the right expertise and experience in order to be well positioned to oversee long term value creation. This includes having directors with diverse backgrounds," so begins PwC's Annual Corporate Directors Survey.¹ The 2016 report offered a shocking finding; 31% of directors believe someone on their board should be replaced. A blistering 15% increase in directors unsatisfied with their colleague's performances since the 2012 survey. This is an indictment on board composition and leadership.

This escalation in dissatisfaction is the culmination of rapidly shifting norms. As globalization has amped up competition, board members too often are selected based on their relationships and connections. As the culmination of Enron and then the global financial crisis shook the core of business, the legal terrain underpinning board governance was rapidly reshaped. And, as the turbulence of proliferating technological



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diffusion has effectively given everyone a computer, smartphone, and internet access in their pocket, boards remain stymied in their reluctance to adopt digital technologies to aid in their efforts in creating sustainable competitive advantage.

In this era, one marked by Big Data and ever increasing digital transformation, a strategy needs to be deployed to ensure corporate governance can stay ahead of the competition and next systemic threat. It must be recognized that the performance of a board of directors is directly tied to their ability to adapt and create synergies in skills and experiences – to create value and competitive advantage.

¹ <http://www.pwc.com/us/en/corporate-governance/annual-corporate-directors-survey.html>

A Growing Call for Re-evaluating Board Composition

Directors are increasingly skeptical of their board's composition

“There are two points on why board composition is critical. One is external,” remarked Tracy Houston, a specialist in board consulting and an executive coach. “It is these external factors that are amplifying the pressure within the boardroom to deliver change. I think the central drivers of turbulence can be attributed to rampant diffusion of technology, increased interdependence across markets, increased shareholder activism, and even frequency of economic shocks,” she continued, “they are driving the demand to retool boards.”

It is important to stress that technological and social change is not new, but the degree and pace have been gaining exponential momentum in the era of the internet and mobile communications. The iPhone was launched in 2007 and the iPad shipped just three short years ago in 2010², and today, there are countless tablets, large phones, and smart devices all around us. And with that, the level of executive acumen necessary in order to capitalize on these new opportunities changed forever. Yet, many companies still use paper or antiquated digital means to distribute materials for board meetings. If your board is not taking advantage of these technologies, how can you keep up with your customers?

The PwC's Annual Survey focuses squarely on growing recognition that board composition must be reevaluated, “At its core, board composition is under pressure to evolve. In order to be well-posed to oversee long-term value creation, directors know their board needs the right expertise and experience – including directors with diverse backgrounds. Directors also recognize they need to be more focused on CEO and director succession in order to make sustained growth a reality.”³ Among the experiences boards find very important in 2016 are the traditional hallmarks, financial, industry, and operational Expertise. Yet their importance to directors is down modestly since 2012. Growing in salience in the survey data are directors saying gender and racial diversity are very important, standing at 39% and 30% respectively.⁴



of directors say gender diversity is important⁴



of directors say racial diversity is important⁴

² <http://www2.deloitte.com/content/dam/Deloitte/us/Documents/regulatory/us-2014-board-practices-report-final-9274051-12122014.pdf>

³ <http://www.pwc.com/us/en/governance-insights-center/annual-corporate-directors-survey/assets/pwc-2015-annual-corporate-directors-survey.pdf>

⁴ *ibid*

It is precisely the reevaluation of board composition's significance that has moved so many board members to become more openly skeptical of their peer's performance. Since 2012, director's motivation to remove a fellow member has continued to grow sharply. The reasons they cite are:

- Aging has led to diminished performance (up 26%),
- A board member is unprepared for meetings (up 36%),
- A board member does not have the expertise required (up 8%).⁵

Indeed, as directors have become more restless, the number of vacancies on boards are on the rise. Vacancies at public companies have nearly doubled since the financial crisis. Taken together, the survey data tells a story of growing director dissatisfaction of their member's skills in the wake of major technological disruption. Organizations need directors who are not intimidated by change, technology, and new modes of thinking. Directors with a fresh perspective, not beholden to the way business has been traditionally executed.

The Delphi corporation is a prime example of a firm that faced every foreseeable disruption and managed to emerge stronger than ever. Between 2005 and 2009 Delphi's CEO led a turnaround effort that replaced the entire board of directors and led the firm to emerge from bankruptcy. The board was populated by a substantial number of outside directors, former CEOs who too led companies during down periods. Following restructuring of outside ownership and the firm's internal workings, the board turned their focus to staying ahead of rapid technological advancement. They created a new CIO position and followed through in establishing an innovation and technology committee. The result was by 2012 annual revenue rose from \$9 to \$16 billion.⁶ The research into board composition and effectiveness bares out Delphi's plan.

In a study in the Academy of Business and Economic Journal, the authors argue "Many scholars, financial analysts, and investors consider outside directors to be better... than inside directors and studies have found their relationship to be stronger with overall corporate performance and larger shareholder returns." Moreover, a board composition that includes a broad range of experiences and backgrounds has consistently proven advantageous. They go on to argue "A high level of board diversity (both women and minorities) has been found to be positively related to profit levels, greater returns on equity (ROE), larger total returns to shareholders and greater returns on assets." That is, a board that is representative of your customer base is better equipped to sustain long term growth.



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⁵ <http://www2.deloitte.com/content/dam/Deloitte/us/Documents/regulatory/us-2014-board-practices-report-final-9274051-12122014.pdf>

⁶ Boards that Lead page 54-58



Research by NACD's annual board composition assessment bares out this assessment. Their report looked at a variety of factors influencing how boards are navigating this new terrain:

"boards must strive for diverse composition as a means of strengthening their own ability to make wise and informed decisions. In particular, this requires gender, racial, age, and experience diversity to broaden the viewpoints, skills, and backgrounds of the individual board members." One director said, "We are looking outside the traditional definition of 'CEO experience...Another participant encouraged fellow directors to "press our search firms to go a level past the usual specs in order to set us up for future success. Where will the interesting next generation of board leaders be coming from?"

Together the evidence suggests that organizations are taking the need for louder outside voices more seriously. They are substantively committing to smarter and more substantive diversity, to become better equipped to face the challenges of this era. The board of directors needs to reach decisions on an extensive array of subjects. It stands to reason that the headwinds faced by today's businesses are best met by a group with specialized skills and knowledge. Those with a unique understanding of issues such as Big Data, IT, new age security threats, and the growing power of digital marketing channels such as social media. The challenge organizations face when confronted by this reality is how to move forward. The next step is evaluating your board, understanding its strengths, opportunities, and weakness.

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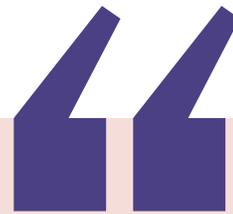
⁷ http://rsmus.com/pdf_download/wp_as_nacd-mcgladrey_director_dialogues_board_composition.pdf

A Path Forward

The opportunity for future-oriented leadership development begins with a wide-ranging evaluation of your current board

The opportunity for future-oriented leadership development begins with a wide-ranging evaluation of your current board of directors. To begin charting a path forward Experts suggest a three-fold response when planning for your board's future.

1. **Start with a broad definition of potential candidates.** There's no need to limit your pool based on personal connections. Indeed, the evidence suggests that a more holistic approach to board recruitment that seeks out diversity of race, age, gender, and experience produce better directors. There's consensus that further board diversity must be a priority:
 - a. 95% of director's view that adding diversity is very much or somewhat important;
 - b. 78% feel that greater diversity enhances board effectiveness, and
 - c. 81% believe it leads to enhanced company performance.⁸



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2. **Utilize a skills matrix to identify skill gaps.** Chart your directors' competencies across a skills matrix, an important tool that assess your current board across skills, background, and experience. Look for overlap, and analyze any gaps. "Those gaps reflect missing competencies that should inform your criteria for new board members," said board governance expert Tracy Houston. A skills matrix can be customized to your organization. [Download this example.](#)

	Board of Directors						
	Name	Name	Name	Name	Name	Name	Name
Term Expiration Date							
Enter Month Year	John Doe						
Skills & Experience							
Belief in/Support of Mission							
Board of Director Experience							
CEO Succession Planning							
Community Affiliation/Access							
Compensation							
Financial							
Fundraising							
Grant Writing							
Human Resources							
(Retail) Industry Knowledge							
Leadership							
Legal							
Lobbying							
Marketing/PR							
Organizational Management							
Risk Management							
Strategic Planning							
Technology/IT							
Comfort w/ Technology							
Demographic Background							
Gender							
Male							
Female							
Age							
25-40							
41-55							
56-70							
Over 70							
Ethnicity							
African American/Black							
Asian, Hawaiian, or Pacific Islander							
White/Caucasian							
Hispanic/Latino							
American Indian							
Other							



3. **Conduct annual evaluations.** In an interview in book *Boards That Lead*, the authors found that “directors are generally comfortable identifying areas where additional expertise would be valuable and where board protocols should be strengthened.” Indeed, board evaluations have surged in recent years, climbing to 90% of all boards. What’s more, roughly half of all companies now have their directors appraise each of their fellow directors. The authors go on to suggest an annual meeting between each board member and the lead director to provide an honest appraisal of the board and individual directors. In certain countries, such as the United Kingdom, laws governing public companies now mandate these annual evaluations. There is a need to plan for these evaluations even if your company is not in one such country, or if you are not a public company.

Surveying your board, identifying gaps by utilizing a skills matrix, and recruiting a diverse set of directors will create environment that encourages open communications, honest evaluations, and strengthen your board’s readiness to fill vacancies when they arrive. Boards should take into account and embrace change in board composition after careful and deliberate consideration.



Roughly half of all companies now have their directors appraise each of their fellow directors

Resources for Creating a More Effective Board

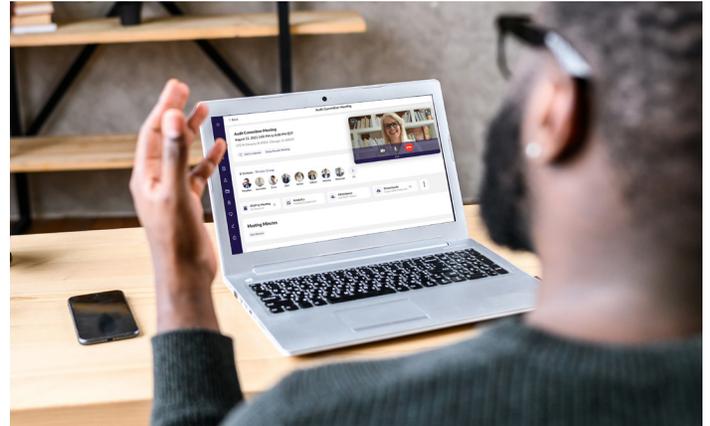
A board portal can drastically improve your board's effectiveness

There are clear, achievable, affordable responses to challenges faced by boards. One example of a powerful technology tool for improving performance are board meeting solutions, often called board portals. These solutions have expanded the opportunity for boards to poll their members, facilitate from board evaluations, and consolidate meeting resources for the creation of in real-time up-to-date distribution of board books.

Apprehension toward technology has become deadweight in board rooms. It has hampered recruitment – the brightest leaders are reluctant to join boards that govern as Luddites. The next generation of leaders, those who are filling the ranks as vacancies accelerate, expect their board of directors to take advantage of productivity and collaboration empowerment technologies such as board meeting solutions. A survey of our customers shows that embracing technology isn't the province of youth.



Apprehension toward technology has become deadweight in board rooms



Larry Rosin, Executive Vice President and Chief Financial Officer for Andigo shared with us that:

“When we approached [the directors] about moving away from pushing paper board packets by electronic means, they were open to it; especially after we explained that the gains in efficiencies, enhanced security, and cost savings were substantial. The board was a bit concerned about not having the paper-packets handy. A 90+ year old director, he has been on our board for going on 50 years, serving as chairman for much of that time.... After he started using the [OnBoard] app, he has never needed paper from us again.”

A digital board portal helps directors become more effective and executive administrators more efficient. A key resource for director to RSVP, access their agendas, conduct approvals, and reference important documents. It would be an understatement to suggest that these tools have revolutionized how board meetings are held. In the same way the internet organized the world's information, board portals have brought a sea change in how board materials are reviewed and created.

Conclusion

More than half of all companies have added a new director in the past year.⁹ So, whether your strategy is to actively replace underperforming members, enlarge your board and bring additional voices to the table, or simply create a succession plan with an eye toward the future, it's critical that the future of your board's composition be considered today. As boards navigate difficult economic pressures, global competitions, an uncertain legal environment, and disruptive technologies, it's critical to get a plan in place and start to execute it immediately to best position your organization and board to create long-term competitive advantage.

The onus now lies with every organization to seriously evaluate whether their board of directors is creating competitive advantage or staffed with insular or uninformed directors. The pressure will continue to mount, and as a new generation of leaders emerges, so too will changes in the board room. Decisions will be made by people who were born using technology, who are culturally comfortable with a new and more robust marketplace of ideas.



**...get a plan in place
and start to execute
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Immediate Opportunity

One crucial way every organization can take a quick step toward positioning their board toward this future is employing board meeting technology. OnBoard, the only solution to offer a free, no obligations, trial with set up requiring less than an hour. With an intuitive interface directors can simply pick it up and start using it with little to no training. To learn more about OnBoard call **765.535.1880** or go to onboardmeetings.com and click **Contact Us** or **Start A Free Trial**.

⁹ <http://www2.deloitte.com/content/dam/Deloitte/us/Documents/regulatory/us-2014-board-practices-report-final-9274051-12122014.pdf>