

# Beyond the CEO

The role of the Board in ensuring organizations have the talent to thrive

How active and effective are Canadian boards in their oversight of human capital risks? What gaps exist and what can be done to close them?

by Knightsbridge Human Capital Solutions and the Clarkson Centre for Board Effectiveness, in partnership with the Institute of Corporate Directors.





# Table of Contents

Executive summary	1
Methodology	3
Survey participant characteristics	4
<b>SECTION ONE</b>	
The ideal board role in the oversight of human capital	5
<b>SECTION TWO</b>	
Board practices and involvement in human capital	7
A) Strategic planning	7
B) Culture and employee engagement	8
C) Executive compensation and performance management	10
D) Succession planning	11
E) Learning and development	13
<b>SECTION THREE</b>	
Common barriers to human capital oversight	15
<b>SECTION FOUR</b>	
Call to action: Enhancing board oversight of human capital risks	17
A) Strategic planning	17
B) Culture and employee engagement	18
C) Executive compensation and performance management	18
D) Succession planning	18
E) Learning and development	19

# Executive Summary

In spring 2011, Knightsbridge Human Capital Solutions (Knightsbridge) and the Clarkson Centre for Board Effectiveness at the Rotman School of Management (CCBE) partnered with the Institute of Corporate Directors (ICD) on a large-scale study into the role and effectiveness of human capital oversight among Canadian boards of directors. Broadly, our goals were to:

1. Understand the role directors believe boards should have in overseeing an organization's human capital. Should they have direct responsibility, a monitoring role, or no oversight at all?
2. Determine what boards are currently doing to identify and monitor various human capital risks, and to what extent their practices are effective.
3. Identify any barriers that exist for boards in providing effective oversight of human capital risks.



Most Canadian directors acknowledge that human capital oversight is an essential part of their work. The vast majority indicated their boards have direct responsibility for CEO compensation, performance management, and development, including succession planning. But the majority of directors also believe that boards should monitor strategic talent management areas such as HR strategy, organizational culture, employee engagement, succession planning, and learning and development.

A majority of directors surveyed believe their organization has the necessary talent to achieve its strategic objectives. But a majority also expressed a desire to spend more time discussing important cultural, leadership, and talent-related risks and challenges facing their organizations. This suggests that directors believe they should be paying more attention to human capital.

Furthermore, based on current board behaviour, directors' confidence in their oversight of human capital may be unfounded. The reality is that many boards either lack the information they need and/or do not spend sufficient time on strategic human capital issues. Responsibilities relating to the CEO, particularly CEO compensation, are currently dominating their human capital discussions.

Beyond the CEO position, we found board involvement in monitoring human capital to be inconsistent. Our study identified opportunities for improving board oversight of human capital in several areas:

- ◆ **Culture and Employee Engagement:** While most organizations share employee engagement survey results with their boards, many boards (42%) do not discuss the results or review management's plans to enhance or maintain employee engagement. In addition, less than half of boards spend sufficient time with employees to assess the culture themselves.

- ◆ **Compensation Beyond the CEO:** Directors focus on CEO compensation, and indicate they are pleased with their progress in this area. However, evidence suggests the structure of compensation plans remains focused on retaining CEOs in the short term, rather than balancing retention and rewarding performance over longer timeframes. In addition, opportunities exist to better monitor compensation plans and their alignment with performance below the executive level, particularly among small- and mid-size companies and not-for-profit (NFP) organizations.
- ◆ **Succession Planning:** Directors say succession planning is important but few organizations have succession plans in place for the CEO and other top executives. Further, there is limited monitoring of succession plans for critical positions below CEO.
- ◆ **Learning and Development:** Many directors believe it is important for boards to ensure their organizations are investing in talent development to enable long-term success, but few directors understand their respective organizations' learning and development strategies. This creates a lack of confidence that high-potential individuals will be sufficiently prepared for succession.

2

## PRIMARY BARRIERS

The primary barriers boards face in overseeing human capital risks are:

1. **Lack of time:** Board meetings are too focused on operational details,
2. **Lack of expertise:** Boards often lack directors with sufficient human capital expertise and/or in the case of smaller organizations, the financial resources to hire external expertise, and
3. **Role alignment:** There is a belief among directors that the board should not oversee human capital beyond the CEO. This is especially true of directors of large NFP boards.

This report highlights these and other important issues facing Canadian boards and demonstrates that there is more work to be done to optimize board oversight of this key governance responsibility.

## Methodology

CCBE collected data for this study using one-on-one confidential interviews and an anonymous director survey. In February and March 2011, CCBE conducted 14 interviews with a diverse group of Canadian directors, focusing on individuals with previous experience overseeing human capital decisions and processes.

The three goals for these interviews were to:

- ◆ Understand what human capital-related risks and issues directors believe boards should be monitoring,
- ◆ Understand what practices are being used to monitor these risks, and
- ◆ Identify any barriers hindering directors from providing sufficient oversight of human capital issues and risks.

3

Feedback from these interviews was used to develop the director survey, which was conducted in April and May 2011.

The director survey gathered quantifiable data from Canadian directors regarding their opinions on the role and state of human capital oversight by Canadian boards. Our survey questions were separated into five topic areas:

1. Participant demographics and board experience,
2. The ideal role of boards with respect to human capital oversight,
3. What boards are doing to mitigate human capital risks,
4. Board meeting time allocation, and
5. Common barriers to effective human capital oversight.

A total of 242 Canadian directors completed the survey, and the CCBE compiled and analysed the data in May 2011. The report authors acknowledge there may be some bias as survey respondents self-selected to participate. This report summarizes our findings and highlights important trends in the strengths and weaknesses of Canadian boards in their oversight of human capital risks.

## Survey Participant Characteristics

Fig. 1: Gender breakdown and board experience

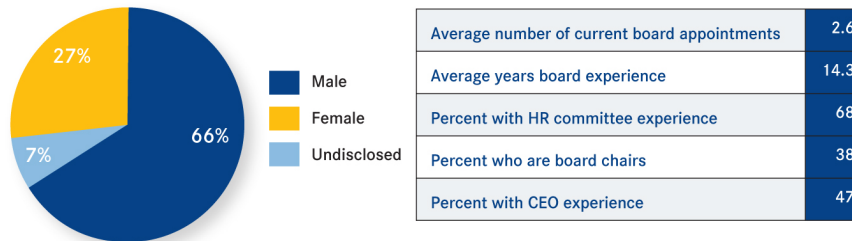


Figure 1—Source, 2011 CCBE/Knightsbridge Human Capital Survey [n=242]

4

Fig. 2: Board experience of participating directors

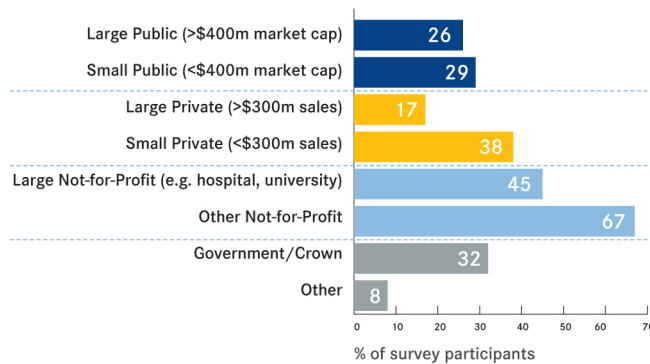


Figure 2—Source, 2011 CCBE/Knightsbridge Human Capital Survey [n=242]

For certain sections of our survey, we asked participants to provide responses with respect to the one board of which they are a director that they believed demonstrated the best oversight of human capital risks. The breakdown of these boards by sector is as follows:

Fig. 3: Board type on which participants based their responses

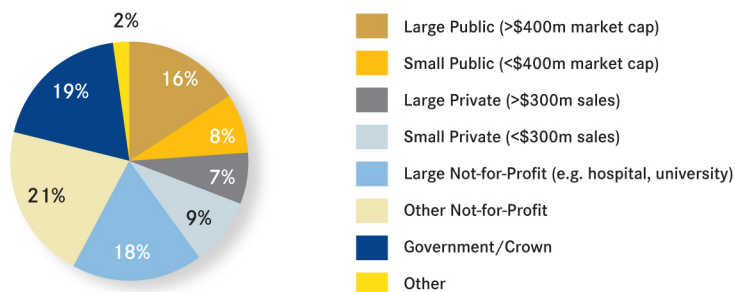


Figure 3—Source, 2011 CCBE/Knightsbridge Human Capital Survey [n=242]

# Section One

## The Ideal Board Role in the Oversight of Human Capital

Canadian directors believe boards are directly responsible for human capital risks relating to the CEO position and ought to provide ongoing monitoring of other human capital risks.

We asked our participants to specify the ideal role for boards with respect to the oversight of five talent-related areas:

1. Human Capital Strategic Planning
2. Culture and Employee Engagement
3. Compensation and Performance Management
4. Succession Planning
5. Learning and Development

Within each of these areas, we asked specific questions about human capital issues and risks. For each question, directors chose from the three options:

1. Boards should be directly responsible
2. Boards should monitor on an ongoing basis
3. Boards should have no oversight role and be completely ‘hands-off’

Not surprisingly, the vast majority of directors indicated that boards should have direct responsibility for CEO hiring, compensation, performance management and development, and succession planning. In addition, most participants believe that boards ought to play an ongoing monitoring role with respect to other talent-related risks. This role includes ensuring boards are aware of talent-related risks and that management has in place sufficiently effective processes and plans to manage these risks.

Our survey results show very little disagreement among sectors and sizes, or among participants with different board roles (e.g. chairs, managers, committee members, etc.). We did, however, identify significant disagreement in two key areas.

**Strategic Planning:** When asked to identify the board’s ideal role in ensuring that the organization’s strategic plan sufficiently addresses talent-related risks and requirements, half (46%) of the participants felt that boards should be responsible for this, while the other half (54%) believed that a monitoring role was more appropriate. We examine this disagreement in more detail in Section 2, Strategic Planning.

**In addition to boards’ direct responsibility for the CEO—including hiring, compensation, performance management and development, and succession planning—most participants believe that boards ought to play an ongoing monitoring role with respect to other talent-related risks.**

5



**Compensation and Succession Below the C-suite:** There is disagreement regarding boards' oversight of compensation and succession planning below the executive level. While a majority of participants believe that boards ought to monitor the compensation plan for the entire organization (65%) and succession planning for critical roles below the executive level (63%), a significant number of directors (24% and 31% respectively) believe that, other than for top executives, these tasks are outside of the scope of board responsibilities (See Figure 4 below).

**Fig. 4: Ideal board role for selected human capital risks**

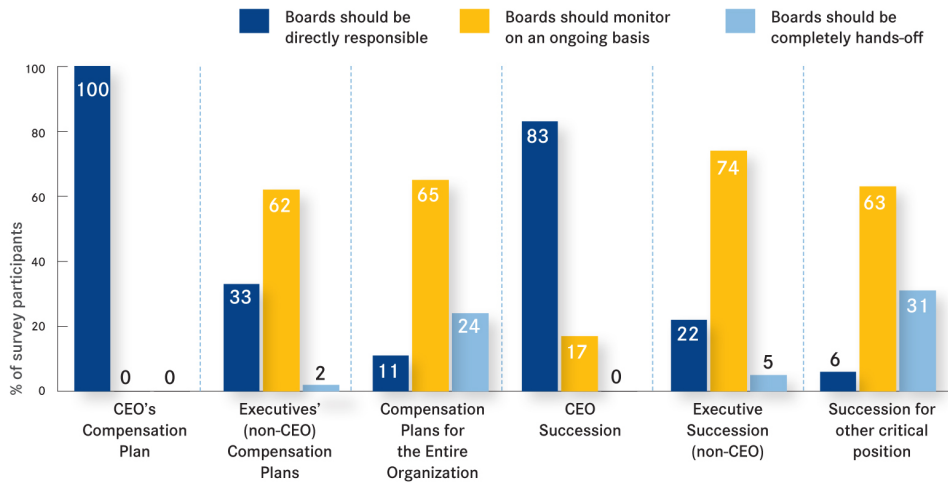


Figure 4—Source, 2011 CCBE/Knightbridge Human Capital Survey [n=242]

Figure 4 - Canadian directors believe boards are directly responsible for human capital risks relating to the CEO position, and ought to provide ongoing monitoring of most other issues.

Boards in all sectors want more meeting time allocated to strategic human capital risks, including discussion related to culture and employee engagement, CEO and executive performance, succession planning, and development and training (See Figure 5). This is consistent with directors' desire to spend more time on strategic planning in general, a trend that has been documented recently by CCBE<sup>1</sup> and in 2004 by the Canadian Coalition for Good Governance and McKinsey (unpublished).

**Boards in all sectors want more meeting time allocated to strategic human capital risks.**

**Fig. 5: Directors are hoping to increase time allocated to human capital topics**



Figure 5—Source, 2011 CCBE/Knightbridge Human Capital Survey [n=242]

<sup>1</sup> CCBE, 2009. Clarkson Centre-PricewaterhouseCoopers 2009 Directors Survey in collaboration with the Institute of Corporate Directors, Toronto.

## Section Two

### Board Practices and Involvement in Human Capital

#### A. STRATEGIC PLANNING

Most directors want to spend more time on strategic talent issues, despite disagreeing on how involved boards should be in ensuring human capital risks are sufficiently addressed in their organizations' strategic plans.

All but one interview participant indicated that boards ought to be responsible for monitoring, and in many cases actively guiding, the organization's strategic plan and ensuring it addresses talent-related risks and needs. However, as mentioned earlier, there seems to be significant disagreement or perhaps confusion with respect to the board's role in ensuring that talent-related risks and requirements are considered as part of the strategic plan.

- ◆ Half of survey respondents (54%) stated that boards should monitor whether an organization's strategic plan sufficiently addresses talent-related risks and requirements (oversight).
- ◆ Almost an equal number (46%) stated that boards should be responsible for ensuring strategic plans address talent-related risks and requirements (direct responsibility).

**Half (54%) of respondents indicated that boards should have oversight to ensure the strategic plan addresses talent-related risks and requirements; the other half (46%) believed boards should have direct responsibility.**

It is interesting to note that participants who endorse direct responsibility are more likely to sit on boards with effective information sharing between the board and management (e.g. employee engagement surveys, exit interviews, etc.) (see Figure 6). However, it is unclear whether this involvement is driven by boards requesting this information, or by CEOs proactively sharing this information for board feedback. The former would suggest that directors who endorse direct responsibility also help to ensure that their boards are fully informed on talent-related issues. The latter would indicate that a voluntary increase in information flow from management helps boards become more engaged in human capital oversight.

**Fig. 6: Percent of respondents confident in employee engagement information sharing between board and management**

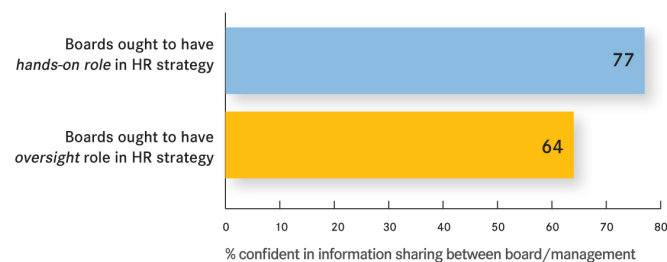


Figure 6—Source, 2011 CCBE/Knightsbridge Human Capital Survey [n=242]

Figure 6 - Participants who think boards should be directly responsible for HR strategy experience better employee engagement information sharing in the boardroom.

Canadian boards generally have a high level of confidence in the effectiveness of their oversight of strategic human capital risks.

- ◆ 75% of participants agree that their company has the necessary talent to achieve its strategic objectives, and
- ◆ 66% of participants are confident that their HR strategic plan contains sufficient detail on key human capital requirements to successfully achieve organizational goals.

**A significant majority (71%) of participants stated that their board receives an organizational HR strategic plan; 70% of boards actively review the plan and provide feedback to management.**

This confidence is likely driven by the fact that a significant majority (71%) of participants indicated their board receives an organizational HR strategic plan; 70% of boards actively review the plan and provide feedback to management.

8

However, it is interesting to note that survey participants who are CEOs or have been CEOs in the past demonstrated notably less confidence than other participants in the effectiveness of the advice and feedback they receive from their boards regarding human capital issues. This may be due to the fact that they are used to seeing more information regarding strategic talent management issues as a CEO, but are not seeing such information and processes shared at the board level.

While the significant majority of directors and boards seem to be effectively overseeing strategic human capital risk, 30% of boards remain under-equipped to assess the effectiveness of their organizations' HR strategies and 25% feel their organizations do not have sufficient talent to achieve key objectives. These figures represent important gaps in the effectiveness of strategic oversight among many of the boards in our sample.

**30% of boards remain under-equipped to assess the effectiveness of their organizations' HR strategies.**

## **B. CULTURE & EMPLOYEE ENGAGEMENT**

While most organizations share employee engagement survey results with their boards, many boards don't discuss the results or review management's plans to enhance or maintain employee engagement. Even fewer boards spend sufficient time with employees to assess the culture themselves.

There is strong agreement among directors in all sectors that the board's role with respect to culture and employee engagement should be one of active monitoring. One director of several private and not-for-profit boards explains, "Boards need information to measure the risks of employee dissatisfaction, but our role here is to understand and suggest, rather than to fix the problems."

Directors give themselves high marks for their effectiveness in overseeing culture and employee engagement. Most say they are highly confident in the effectiveness of their organization's culture, and the majority (72%) believe they

are sufficiently informed to identify important organization-wide cultural challenges and issues, and also to provide guidance where necessary to overcome them.

However, many Canadian boards have not implemented formal processes to ensure effective oversight of culture and employee engagement on an ongoing basis. In most cases (71%), management shares the results of employee engagement surveys with their boards. But only 58% of boards actually discuss these results and provide feedback to the management team (see Figure 7 below). Only 49% of boards spend any time with employees to understand the organization’s culture.

**Fig. 7: Many boards don’t discuss employee engagement**

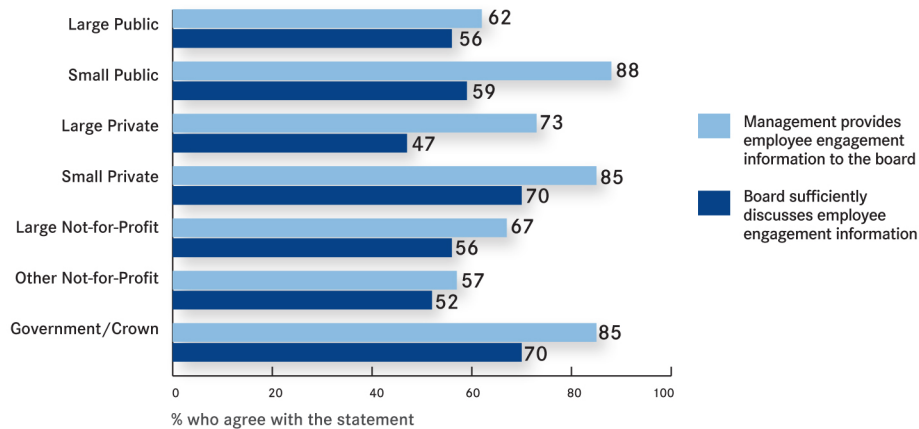


Figure 7—Source, 2011 CCBE/Knightsbridge Human Capital Survey [n=242]

Figure 7 - Although a majority of boards across sectors receive information from management regarding employee engagement, many are not taking the time to sufficiently discuss the information they receive.

This indicates that although there is widespread desire for boards to actively monitor cultural issues, many still lack the formal processes to do so effectively. Given that 84% of directors expressed confidence that their boards would openly voice concerns relating to culture, it may be that directors believe it is only necessary to pay attention to organizational cultural issues when they arise. Another possible explanation is that without sufficient practices in place to monitor the organization’s culture on an ongoing basis, boards only learn of issues after damage has been done.

It is important for boards to ensure appropriate cultural oversight, as cultural challenges can have important strategic repercussions. As one director of several large public boards states, “Directors need to ask if they’ve identified all the key [cultural] risks. We have a strong influence over culture—after all, we hire the CEO.”

**“The number one thing a board can do is to foster a very transparent line of communication between the board and management. This is the ideal [cultural role]: setting the tone at the top.”**

Director with experience on several private and government boards

### C. EXECUTIVE COMPENSATION AND PERFORMANCE MANAGEMENT

While boards pay close attention to CEO compensation, evidence suggests the structure of compensation plans remains more focused on retaining CEOs in the short term, rather than balancing retention and rewarding performance over longer timeframes. Also, opportunities remain to better monitor compensation plans and their alignment with performance below the executive level.

In our preliminary interviews, executive compensation challenges were among the most pressing human capital issues facing Canadian directors. With ever-increasing scrutiny from investors, media and other external sources, and increased pressure to optimize pay/performance alignment in the long-term, boards are seeking to identify and implement processes and structures to meet external expectations as well as internal realities.

As expected, all directors believe CEO performance and compensation is the direct responsibility of the board, regardless of sector and size. Similarly, 95% of participants believe that boards ought to play at least a monitoring role regarding the compensation of senior executives below the CEO level, and three-quarters believe directors should monitor the performance and compensation policies for all employees. It is clear that Canadian directors are fully embracing their role as stewards of compensation and performance.

**95% of participants believe that boards ought to play at least a monitoring role regarding the compensation of senior executives below the CEO level, and three-quarters believe directors should monitor the performance and compensation policies for all employees.**

The survey results indicate widespread adoption of formal board processes to monitor performance and make decisions regarding CEO compensation:

- ◆ 87% of participants are confident that their pay levels have enabled them to attract and retain appropriate and effective CEO candidates,
- ◆ 83% feel that these pay levels are consistent with stakeholder expectations, and
- ◆ 79% of directors believe they have been successful in crafting appropriate CEO performance objectives that have a meaningful impact on pay levels.

However, recent CCBE research indicates that while many organizations manage to successfully align pay and performance in any given year, individual companies often struggle to maintain ongoing pay/performance alignment under even modest year-over-year performance fluctuations. This suggests that our survey participants' boards are likely only focusing on pay/performance alignment over short time horizons (e.g. one to two years). This hypothesis is further bolstered by the fact that only 9% of firms listed on the S&P/TSX Composite Index currently have performance requirements for the vesting of executive options, and few have implemented other policies/practices designed to ensure long-term pay/performance alignment (see Figure 8). It appears that many boards still view CEO pay for performance more as a retention tool rather than as an incentive to achieve important strategic objectives.

**Fig. 8: S&P/TSX composite index adoption of long-term pay/performance alignment policies**

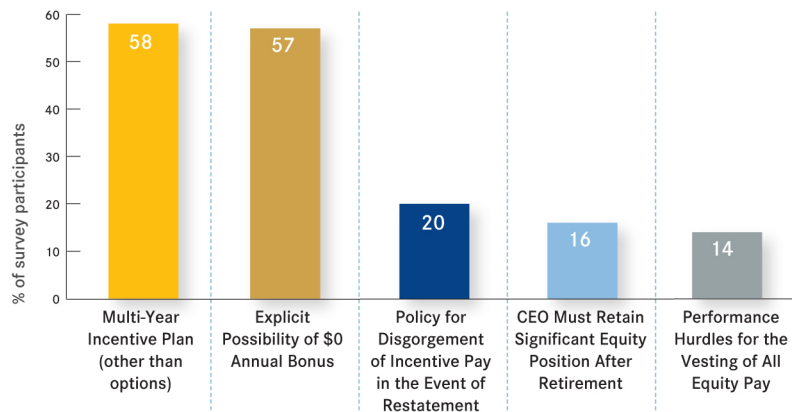


Figure 8—Source, CCBE 2010 Board Shareholder Confidence Index

Figure 8 - Many large Canadian firms have not adopted policies/practices to ensure long-term pay/performance alignment.

While many boards (41%) do not use formal evaluation tools to measure CEO performance (e.g. 360° evaluations and other assessment vehicles), most of our participants (79%) are confident that their processes for performance oversight and feedback are effective, and that they are able to provide effective guidance in times of underperformance (68%). In addition, most of our participants (68%) are satisfied with the amount of time they spend in board meetings discussing CEO performance, and also believe that they have sufficient time to discuss CEO pay (81%). Small not-for-profit boards are struggling to ensure regular meaningful discussion regarding CEO performance, with 37% expressing low confidence in their boards' performance review processes.

**Small not-for-profit boards are struggling more than other boards to ensure regular meaningful discussion regarding CEO performance, with 37% expressing low confidence in their boards' performance review.**

Finally, our participants indicated that there is room for improvement in their processes for monitoring performance and compensation below the executive level. Survey respondents, particularly among small and medium-sized enterprises (SMEs) and not-for-profits, felt they are not sufficiently reviewing compensation risks throughout the organization. This challenge is most prevalent among small NFPs, where 46% of participants expressed low confidence in their organization-wide monitoring of compensation and performance.

#### D. SUCCESSION PLANNING

Despite significant agreement about its importance, few organizations have succession plans in place for the CEO and other top executives, and there is limited monitoring of succession plans for critical positions below CEO.

Interview participants identified executive succession planning as the second most important human capital concern facing Canadian boards, after CEO compensation. Both interview and survey participants indicated nearly

unanimously that succession planning, particularly at the CEO level, is the board's most critical direct responsibility. Despite this agreement, only 83% believe boards are responsible for ensuring that suitable successors to the CEO position are identified at all times. The remainder believe succession planning is only necessary when the CEO has left or is planning to leave.

Despite its stated importance, many boards seem unsuccessful in implementing CEO succession plans. Although 86% of new CEOs hired by S&P/TSX Composite Index firms in 2009 were *internal hires*<sup>2</sup>, suggesting successful succession planning, only 55% of survey participants agree that their boards have in fact identified suitable CEO successors (see Figure 9). Only 40% are confident their current succession plan will ensure seamless leadership under unexpected circumstances.

**Fig. 9: Only large public and large private organizations are likely to have formal succession plans in place**

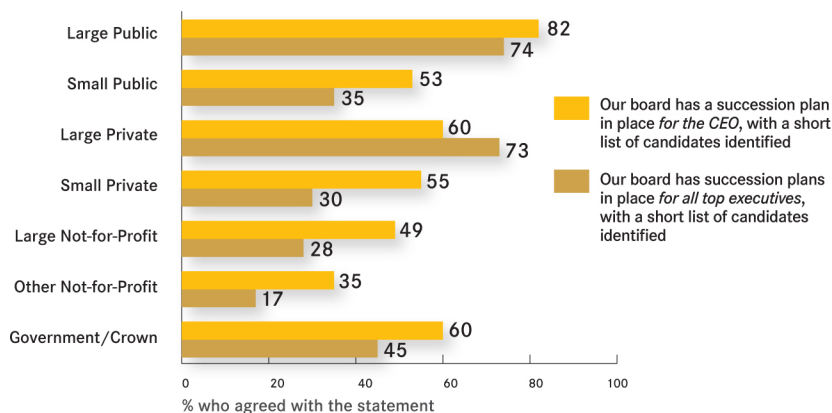


Figure 9—Source, 2011 CCBE/Knightbridge Human Capital Survey [n=242]

Figure 9 - Many boards across all sectors currently have not identified potential successors for executive positions.

In hundreds of one-on-one interviews with Canadian directors in recent years CCBE has often heard that incumbent CEOs can present a cultural hurdle to succession planning. Many directors we interviewed indicated their boards are hesitant to broach the subject of succession planning for fear they may undermine their CEO's trust and confidence. In some cases, succession discussions have failed entirely due to the CEO's refusal to participate.

However, our survey results seem to contradict these previous findings. Most survey participants (72%) stated that their CEO is supportive of board succession endeavours, even if they are not planning to leave. Furthermore, 61% of directors indicated that their CEO works with the board to identify successors for other top executive positions. This contradiction indicates either that participants' confidence in this area is overstated, or that boards are just beginning to put more emphasis on succession planning. Perhaps boards are becoming less concerned about offending CEOs, or perhaps CEOs in general are becoming more engaged in the succession process.

2. 19 of 22 new CEOs according to the Clarkson Centre's 2010 Board Shareholder Confidence Index

In terms of succession planning for executives and other critical positions below the CEO, directors believe they should have a monitoring role to ensure processes and plans are in place to maintain the successful operation of the organization. However, the directors surveyed are concerned about their ability to fill this role. While 65% are confident their organizations allocate sufficient time to identifying high-potential internal candidates for executive positions:

- ◆ Only 39% believe they have identified suitable successors for all executive positions,
- ◆ Just 38% are confident in the ongoing quality of executive succession (see Figure 9),
- ◆ About half (47%) do not review the organization's processes or succession plans for high-potential candidates for key positions, and
- ◆ Only 41% believe their management teams give them enough information to assess the effectiveness of succession plans for critical positions below the executive level.

13

As a result, only 54% of directors are confident that their organizations will continue to have effective staffing in key non-executive positions.

These significant gaps indicate an improvement opportunity for Canadian boards in the oversight of succession planning, both for CEOs as well as executives and other critical positions. As a result, it is not surprising that 44% of respondents indicated that their boards would benefit from a further increase in time allocated to succession planning in general.

## E. LEARNING AND DEVELOPMENT

Few directors have a good understanding of their organizations' learning and development plans, resulting in a lack of confidence that high-potential individuals will be sufficiently prepared for succession.

The majority of directors surveyed expressed interest in improving their understanding and oversight of employee learning and development:

- ◆ A great majority (89%) believe the board is directly responsible for ensuring the CEO has sufficient coaching,
- ◆ 85% believe boards should be monitoring the effectiveness of development for all top executives, and
- ◆ 68% believe they should have oversight of leadership development plans/programs for high potential individuals and critical managers.

**Only 67% of respondents say they spend sufficient time ensuring the CEO has the coaching and support he or she needs to be successful, and only 64% state that their organizations have formal training programs of any kind in place for top executives.**

Despite strong agreement with respect to boards' responsibility for CEO development, and oversight of the development of top executives, only 67% of respondents say they spend sufficient time ensuring the CEO has the coaching and support he or she needs to be successful, and only 64% state that their organizations have formal training programs of any kind in place for top executives.



In addition to active board engagement in overseeing CEO development, many survey participants (54%) believe their boards would benefit from an overall increase in time allocation to executive development in general. Only 47% of directors feel they have adequate access to data regarding the strengths and weaknesses of their executive teams. This leaves a majority of boards at a disadvantage when it comes to providing input into succession and development plans (see Figure 10).

**Fig. 10: Most boards struggle to obtain and discuss learning and development information**

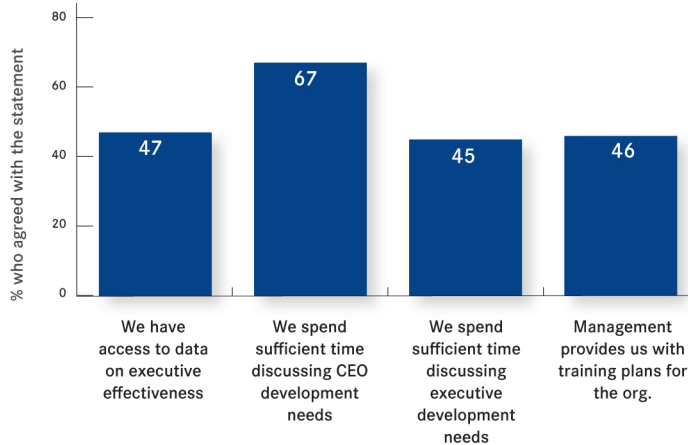


Figure 10—Source, 2011 CCBE/Knightsbridge Human Capital Survey [n=242]

Figure 10 - Boards in all sectors indicated a need for further information and discussion of executive development.

Finally, although more than two-thirds of directors feel that their boards ought to monitor the organization’s processes and progress in the development of high-potential candidates for critical positions, most are failing to do so in practice. Nearly half of all boards (47%) are not monitoring the development of anyone other than the CEO. A majority (60%) provide no oversight of learning and development at the organizational level. Therefore, it is not surprising that only a small majority (56%) of directors are confident that their high-potential candidates will be sufficiently prepared for succession, and that their key executives will continue to be effective on an ongoing basis. This confidence gap presents a crucial governance risk.

**Nearly half of all boards (47%) are not monitoring the development of anyone other than the CEO. A majority (60%) provide no oversight of learning and development at the organizational level.**

**“The development of middle management is a major issue [because] people are not naturally managers. Training people to make sure they are working together well seems very basic, but is highly critical!”**

Director and executive of a provincial government agency

## Section Three

### Common Barriers to Human Capital Oversight

In our survey, we provided participants with a list of potential obstacles to the successful oversight of human capital risks and asked them to indicate how common these barriers are to Canadian boards.

Approximately half of participants stated that boards don't see human capital as a priority and suggested that their board colleagues commonly feel they are not responsible for human capital oversight. Only directors on public and large private boards are confident their boards have embraced their human capital oversight responsibilities. Most notably, 62% of large not-for-profit participants are concerned that their boards do not believe they are responsible for human capital oversight at all (see Figure 11).

**Approximately half of participants stated that boards don't see human capital as a priority.**

15

**Fig. 11: Participants who stated boards don't believe they are responsible for human capital oversight**

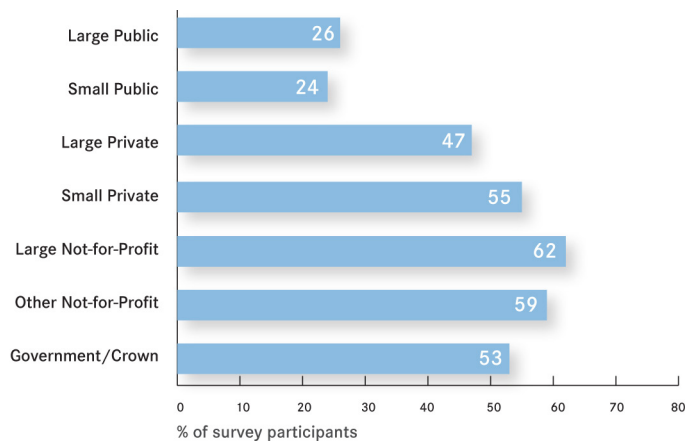


Figure 11—Source, 2011 CCBE/Knightsbridge Human Capital Survey [n=242]

Figure 11 - Many directors struggle with boards that do not believe they are responsible for human capital oversight.

A lack of CEO support can also be a significant barrier. 62% of respondents agreed that the CEO and management team feel threatened when the board gets too involved in human capital issues and risks. This reinforces the need to further clarify the boards' role in the oversight of an organization's human capital.

**62% of respondents agreed that the CEO and management team feel threatened when the board gets too involved in human capital issues and risks.**

Lack of expertise in human capital issues and practices is even more prevalent. 65% of our participants indicated that boards and/or executive teams commonly lack sufficient expertise to effectively handle talent-related challenges. The same number of participants believe that

boards often do not have access to sufficient financial resources to fully equip themselves (through education, outside advice, etc.) to provide valuable human capital guidance.

Time constraints—cited by 69% of survey participants—are the most significant barrier to effective board oversight of human capital. Directors confessed that their board and committee meetings are often too focused on operational minutiae to allow time for forward-looking strategic discussions about talent throughout the organization. As mentioned earlier, boards would like to increase the time allocated to discussing organizational culture, HR strategy, succession planning, and employee development.

**Time constraints—cited by 69% of survey participants—are the most significant barrier to effective board oversight of human capital.**

**Fig. 12: Percent of participants who commonly encounter barriers to effective human capital oversight**

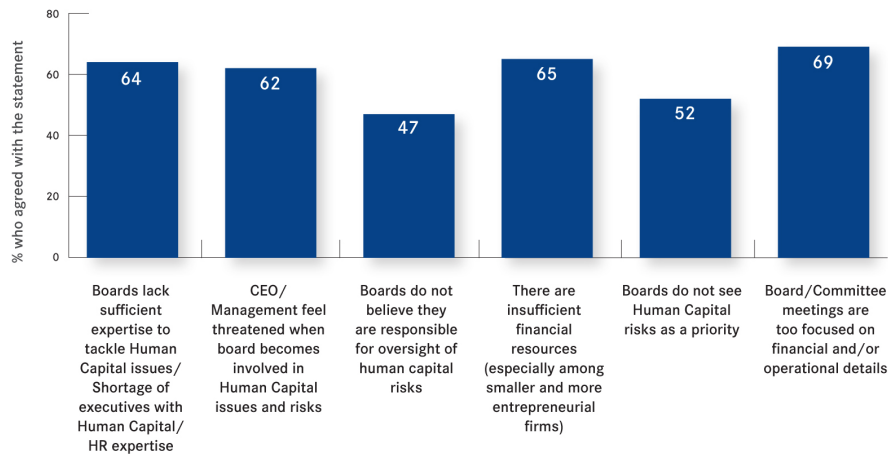


Figure 12—Source, 2011 CCB/E/Knightbridge Human Capital Survey [n=242]

Figure 12 - The most common barriers to effective board oversight of human capital are time constraints, insufficient resources and a lack of board expertise.

The solution, however, may not be as simple as increasing the number or length of board meetings. Rather, a broad shift in board routines may be needed to move focus from backward-looking operational details to forward-looking strategic guidance, including each of the human capital topics discussed in this report. Although board processes are frequently rooted in many years of formality and routine, there is evidence that Canadian directors are hoping for meaningful change.

## Section Four

### Call to Action: Enhancing Board Oversight of Human Capital

Since human capital issues and risks are often a function of an organization's industry and size, the human capital priorities and the processes used to monitor human capital risks will vary from board to board.

That said, there are certain steps that boards as a whole, and directors as individuals, can take to enhance their oversight of human capital to mitigate risk and ensure their organization has the culture and talent it needs to be successful. These include:

17

1. **Surface the issue:** Discuss as a board, and get CEO alignment on the top three to five critical human capital risks facing the organization and how the board can monitor these risks effectively.
2. **Allocate time:** Ensure sufficient time is allocated in every board meeting to discuss the most critical human capital issues facing the organization. Boards should consider establishing an annual cycle that enables the board to regularly and sufficiently monitor and discuss compensation, culture and employee engagement, succession planning, talent development and other key human capital topics throughout the year.
3. **Expand the role of the HR Committee:** The HR Committee should focus their time equally on talent development and compensation. Ensuring an organization has the leadership and talent required to create competitive advantage has as much impact, and sometimes more, on performance than compensation. The HR Committee should work with management to ensure that the organization is adequately focused on assessing and developing firm-wide culture and leadership, and providing the appropriate materials to update the board. In larger organizations, it is often best practice to have a full time executive responsible for Talent, who reports to the Head of HR and can work directly with the HR committee.
4. **Ask specific questions:** Directors can ask the following questions or request information on each of these areas to improve oversight effectiveness:

#### A) STRATEGIC PLANNING

- ◆ What human capital challenges or risks are we most likely to face in executing our strategic plan?
- ◆ Given the organization's strategy and future challenges, what are the leadership requirements needed for successful execution? What current leadership requirements must be preserved? What leadership requirements must be developed or acquired?

- ◆ How will we know if we have the right number of people and/or the right mix of leadership and technical skills to execute the strategy at all levels throughout the organization? What is our process for measuring the capability of our workforce, and identifying and quantifying any gaps we might have?
- ◆ If we have capability gaps, how will we address them? What potential barriers exist in attracting the talent we require, and how will we overcome these barriers?
- ◆ How can we be sure we have the culture, leaders, and processes required to implement our strategy?

## B) CULTURE AND EMPLOYEE ENGAGEMENT

- ◆ What type of culture (values and behaviours) do we want or need to be successful? To what extent is the culture we want being demonstrated within the organization and the board? Are we reinforcing, recognizing and rewarding the values and behaviors we want to encourage?
- ◆ What are the organization's processes for monitoring culture and employee engagement? Do they provide employees with ample opportunities to offer feedback on the organization's leaders (e.g. through surveys, 360° reviews, exit interviews, etc.)?
- ◆ What process and plans does the organization have in place to act on the findings of cultural assessments and employee engagement surveys?
- ◆ Are there opportunities for the board to interact with employees? Holding board meetings in different offices/locations and/or arranging tours of operations during which directors can meet and speak with employees informally are ways to create such opportunities.

## C) COMPENSATION AND PERFORMANCE MANAGEMENT

- ◆ How do the performance objectives of our key executives align with our strategic goals?
- ◆ Have we scenario-tested the compensation plan of the CEO and top executives to ensure that the outcomes are reasonable and aligned to our strategic goals, the expectations of our shareholders or stakeholders and our risk appetite?
- ◆ What is the compensation and incentive philosophy or plan for all critical roles throughout the organization? How does it balance the ability to attract or retain the calibre of talent the organization requires with the company's strategic goals and stakeholder expectations?
- ◆ Do the organization's compensation plans effectively balance short-, medium- and long-term objectives and incentives to ensure pay/performance alignment long term?

## D) SUCCESSION PLANNING

- ◆ Has the board worked with the current CEO to identify a shortlist of his/her potential successors? If not, why not? What barriers exist, and how can they be addressed?
- ◆ Has management identified potential successors for all leadership and critical positions? If so, are the successors currently ready to step into these roles? If not, what are the gaps in their development and what plans are in place to address these gaps?
- ◆ Does the board know the high potential executives and managers below the management team? Are there opportunities for high potential executives and managers to meet and interact with board members via board presentations, informal meetings, department tours, or lunches and dinners?
- ◆ Do the organization's succession plans take into consideration the diversity of backgrounds, skills, and experiences needed to create a balanced organization that understands the needs of its customer base?

19

## E) LEARNING AND DEVELOPMENT

- ◆ How much does the organization invest in learning and development, and how does it compare with industry leaders or best practice organizations?
- ◆ Has the organization developed a comprehensive learning path for high potential individuals that provides them with the cross-functional and leadership experience required to be a successful executive? Does the CEO play an active role in leadership development; ensuring its prioritization and encouraging the movement of high potential individuals throughout the organization to avoid hoarding by specific business units or functions?
- ◆ What are the key leadership, management, and technical skills required to effectively execute the organization's strategy? To what extent does the current organization possess these skills, and what if any gaps exist?
- ◆ What plans are in place to address key skill gaps?

**Summary:** For the most part, our research participants agree on the need and importance of improving board oversight of human capital risks. To translate this recognition into action that improves governance, directors will need to:

1. Surface the issue within their organizations,
2. Build time for human capital oversight into their boards' schedules,
3. Decide on the appropriate scope of human capital oversight for their own organizations, and
4. Identify priorities, develop and implement effective processes for overseeing human capital risks.

This is a tall order, but the stakes are equally huge. Canada's ability to compete successfully in an increasingly competitive global economy depends on the strength of the people leading and managing our organizations.



**Knightsbridge** works with organizations to help them seamlessly execute their strategy through people. Teams of experienced specialists in Leadership & Talent Development, Executive Search & Recruitment, Career Development & Transition, and Workforce Management provide integrated solutions to deliver on your human capital needs. Knightsbridge has the people and services you need when you need stronger people.

Knightsbridge is Canada's fastest growing human capital company, with 25 offices and 265 employees across Canada, the U.S and the U.K., including Toronto, Montreal, Ottawa, Calgary, Vancouver, as well as Halifax, Moncton, and St. John's through our strategic alliance with Knightsbridge Robertson Surette. We serve our clients globally through strategic alliances with Lee Hecht Harrison for career transition services and Amrop for global executive search.



**The Institute of Corporate Directors** (ICD) is a not-for-profit, member-based association representing Canadian directors and boards across the for-profit, not-for-profit, and government sectors. With more than 5,000 members and a network of nine chapters, the ICD promotes the effectiveness of directors by providing quality director education and professional certification; opportunities for continuous learning and networking through local chapter events; board matching and referral service; and access to timely information on current and emerging governance issues and best practices.



**The Clarkson Centre for Business Ethics and Board Effectiveness** (CCBE) is the locus of corporate governance research and communications at the Rotman School of Management. Our mandate is to monitor Canadian corporate governance trends and to provide guidance to firms looking to improve their board effectiveness and disclosure. Current CCBE research focuses include CEO compensation disclosure, a study of small and medium-sized enterprises' governance, and tracking the governance impact of Directors who sit on the boards of four or more TSX Index-listed companies. Since 2002, CCBE's annual Board Shareholder Confidence Index has become the standard by which Canadian governance best practices are measured. The BSCI ratings and other current Clarkson Centre publications are available at [www.rotman.utoronto.ca/ccbe](http://www.rotman.utoronto.ca/ccbe).

# Beyond the CEO

The role of the Board in ensuring  
organizations have the talent to thrive

by Knightsbridge Human Capital Solutions  
and the Clarkson Centre for Board Effectiveness,  
in partnership with the  
Institute of Corporate Directors.

RESEARCH REPORT | SEPT 2011