Diligent Institute

Beyond the C-Suite: Trends in Director Skill Sets

JULY 2021 DILIGENTINSTITUTE.COM

About Diligent Institute

Diligent Institute seeks to help corporate leaders be more effective by providing cutting-edge insights on corporate governance, by amplifying the voices of diverse corporate leaders, and by sharing broadly all that we are learning about modern governance practices.

Founded in 2018, Diligent Institute serves as the global corporate governance research arm and think tank of Diligent Corporation, the largest SaaS software company in the Governance, Risk and Compliance (GRC) space. We produce original research both on our own and in collaboration with partners, including institutions of higher education and thought leaders in the corporate governance space. We produce over a dozen reports each year, ranging from our monthly Director Confidence Index, which measures how corporate directors are feeling about the economy, to in-depth reviews of issues such as ESG (environment, social, governance) practices, to our AI-powered Corporate Sentiment Tracker that analyzes data from thousands of public sources to discern what's on the minds of corporate leaders. Diligent Institute is funded solely by Diligent Corporation.

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About Diligent

Diligent is the largest governance, risk and compliance (GRC) SaaS provider, serving more than one million users from over 25,000 organizations around the globe. Our modern GRC platform ensures boards, executives and other leaders have a holistic, integrated view of audit, risk, information security, ethics and compliance across the organization.

Diligent brings technology, insights and confidence to leaders so they can build more effective, equitable and successful organizations. We empower 79% of the Fortune 500, 90% of the FTSE 100 and 83% of the ASX 200 to improve their bottom line, to keep pace with stakeholder expectations and to create a lasting, positive impact on the world.

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Background

Shifting Priorities Require New Boardroom Talent

The COVID-19 pandemic has been the catalyst of unprecedented changes to the business landscape. Issues that were trending even before the pandemic have been accelerated to the top of board agendas, including workforce policy, talent recruitment and retention, digital transformation, cybersecurity, brand and reputational risk, ESG and DEI, to name a few.

These trends are being reflected in changes to board member recruitment practices, as boards felt pressure to augment their existing talent pool with new directors with different skill sets and experiences. In Diligent Institute's December 2020 Ask a Director[1] series, board members expressed a desire to increase their boards' adaptability to face new challenges, particularly by ensuring that the voices around the table came from diverse backgrounds and represented a wider array of skillsets. Then, in a Diligent Institute and Corporate Board Member joint report called What Directors Think[2], directors indicated that skillset and background diversity was more important in the selection of their next board member than CEO experience for the first time in the survey's 18-year run.

The message coming from directors was clear: they see "cognitive diversity" (different ways of thinking) in the boardroom as a strategy to successfully navigate crisis and change. Diligent Institute set out to measure whether these sentiments are translating into new director recruitment and appointments. In other words, are boards actually appointing directors from nontraditional professional backgrounds?

Methodology

To better understand current practices, we worked with the research team at CGLytics, a Diligent brand, to analyze data on public company board appointments globally. We reviewed 4,300 public companies headquartered in the United States (US), the United Kingdom (UK) and Australia (AUS) for comparison, analyzing new director appointments made from January 1, 2019 through May 31, 2021.

For the purposes of this study, directors with "traditional backgrounds" are defined as those who have held the role of CEO, CFO or COO. Directors with "nontraditional backgrounds" are defined as those who have never held those roles, but have other professional backgrounds, including leadership roles in technology, marketing, sales, legal, human resources (HR) or a role related to environment, social or governance (ESG). Finally, we analyzed the data set for any gender differences.

1. Ask a Director: What Lessons Have Boards Learned from COVID-19? report by Diligent Institute.
2. What Directors Think, report by Diligent Institute and Corporate Board Member, pg. 8.

Key Takeaways

- The share of newly appointed directors who come from a traditional CEO/CFO/COO background is declining – dropping from 59.4% to 56.0% since 2019.

- Over the same time period, the share of newly appointed directors who come from non-traditional backgrounds has increased from 13.0% to 18.9%.

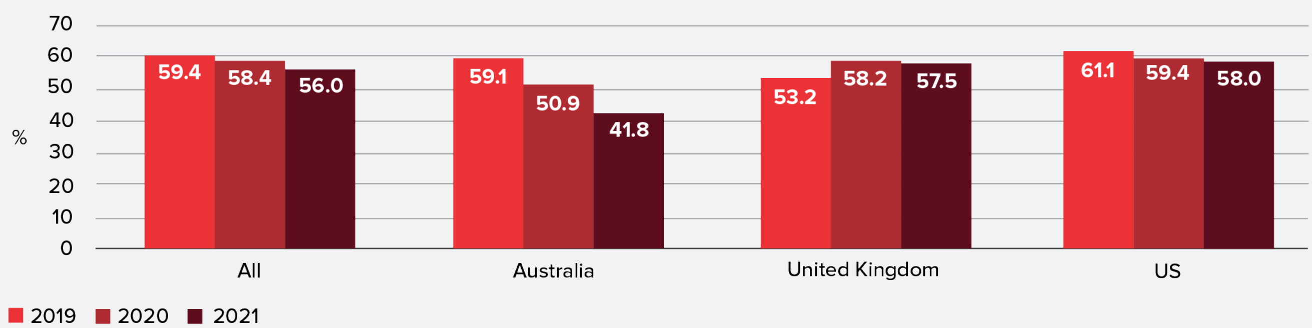
- The group of newly appointed directors with nontraditional backgrounds is split almost evenly along gender lines. However, newly appointed directors from CEO/CFO/COO backgrounds are twice as likely to be men, while women represent the majority of new appointments in technology and marketing, and the vast majority of new appointments in HR and ESG.

Analysis

Differences in New Director Expertise by Country

Across the three countries included in our sample, the share of newly appointed directors with traditional backgrounds has been steadily declining each year. Since 2019, the number of directors who have CEO/CFO/COO experience declined from 59.4% to 56.0% of new appointments over that period.

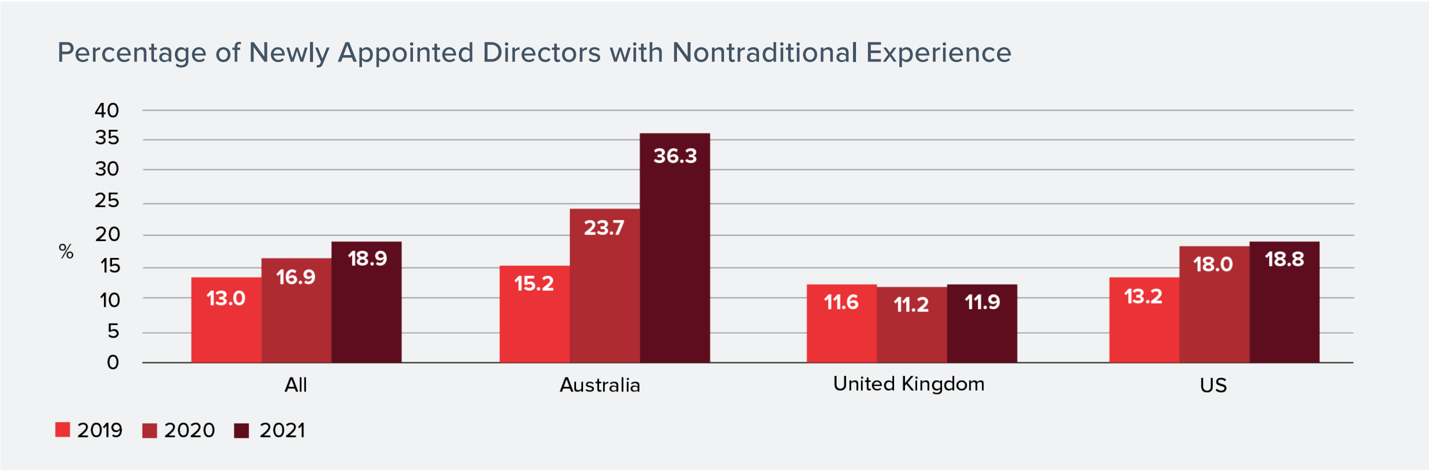
Percentage of Newly Appointed Directors with CEO/CFO/COO Experience



The most dramatic shift has occurred in Australia, which has dropped from 59.1% traditional board appointments in 2019, to 41.8% in 2021 – a 30% decline. The US has declined at the average pace from 61.1% in 2019 to 58.0% in 2021.

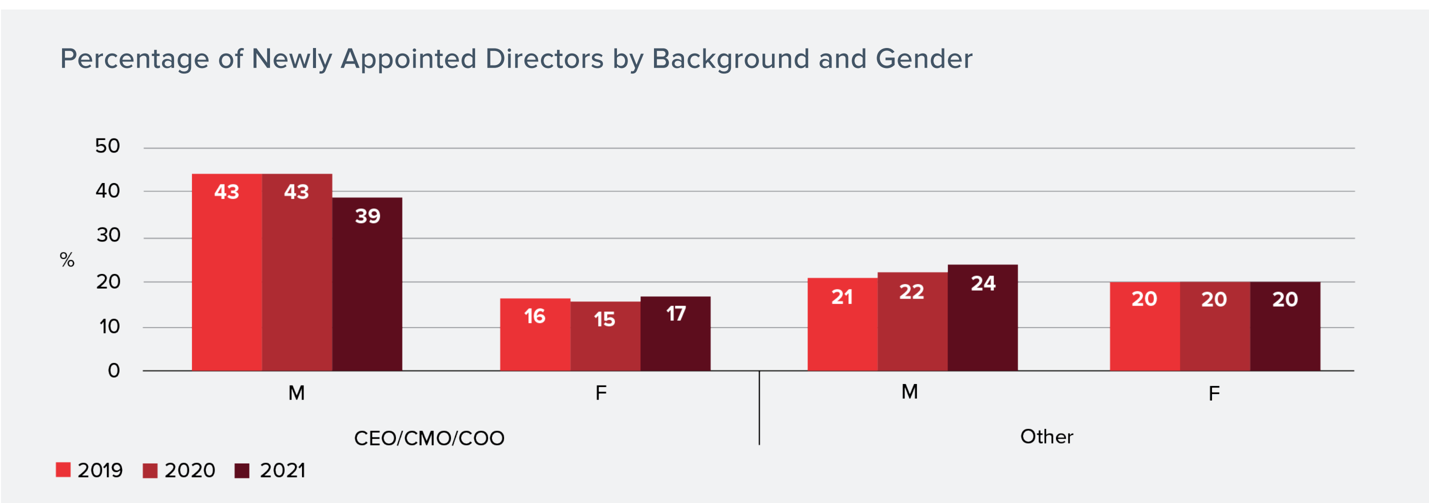
Interestingly, the picture in the UK is mixed: new appointments from traditional backgrounds rose slightly between 2019 and 2020, then fell in the first half of 2021 to 57.5%.

The following chart looks at the percentages of new director appointments in this sample who have exclusively nontraditional backgrounds (marketing, sales, legal, HR, technology and ESG). The overall share of new director appointments with nontraditional backgrounds is on the rise, increasing from 13.0% in 2019 to 18.9% in 2021 – a 45% increase.



Again, the most pronounced results are in Australia: nontraditional appointments comprised of 15.2% of all new director appointments in 2019 and had more than doubled by 2021 at 36.3%. The US is aligned with the global average, with nontraditional director appointments rising from 13.2% in 2019 to 18.8% in 2021. In the UK, there has been little change with nontraditional board appointments hovering just below 12% in each year of our sample.

Directors with CEO/CFO/COO Experience Twice as Likely to be Men

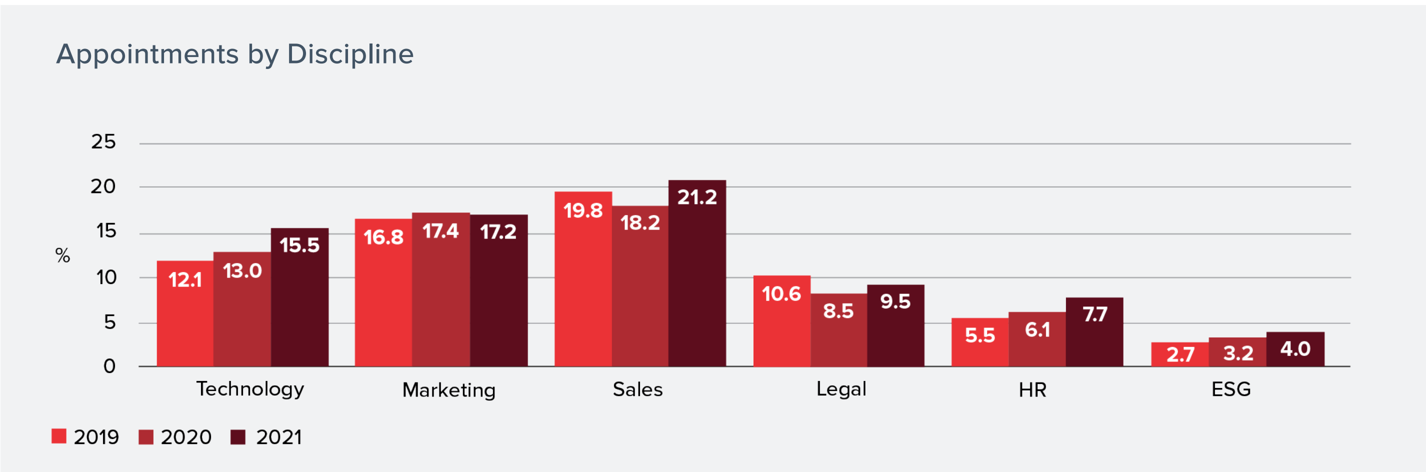


When broken down by gender, we see that the proportion of newly appointed directors who are males with traditional backgrounds has decreased slightly over the last two and a half years, dropping from 43% in 2019 to 39% in 2021. The proportion of females from traditional backgrounds has remained about the same, hovering between 15-17%.

By contrast, the share of new director appointments who are males with nontraditional experience has increased slightly from 20% to 24% over the two-and-a-half-year span. The share of new director appointments who are females with nontraditional backgrounds has held steady at 20%.

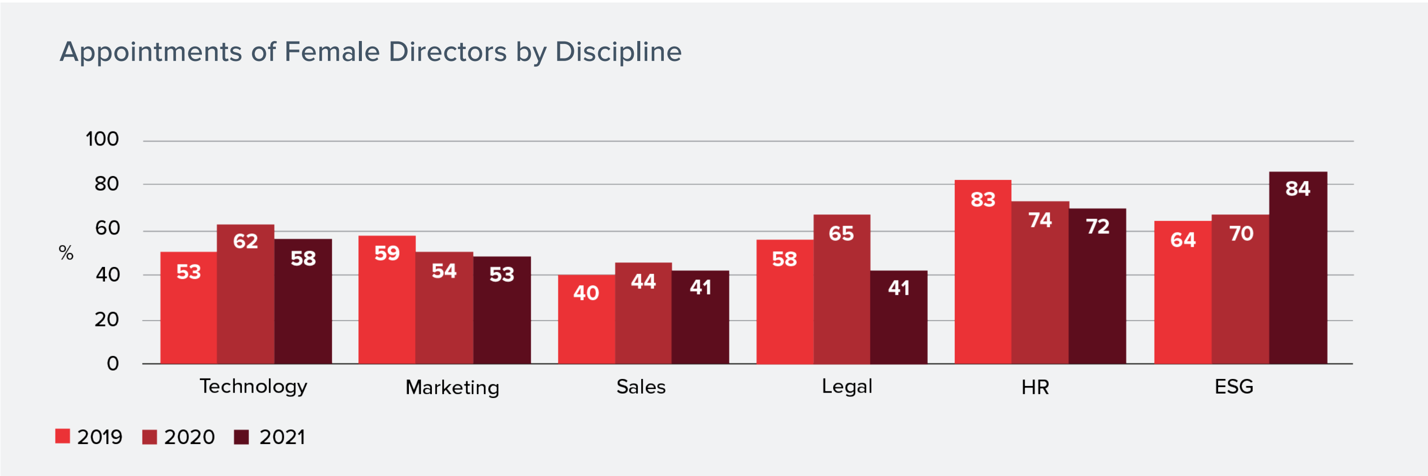
Interestingly in this sample, appointments of directors from nontraditional backgrounds are at near gender parity, whereas directors from traditional backgrounds are twice as likely to be male as female.

Trending Areas of Expertise for New Director Appointments Include Technology, Marketing, Sales and Legal, with HR and ESG on the Rise



When looking at the breakdown of new appointments by discipline, we can see that the share of those with technology, HR, and ESG experience is on the rise. Since 2019, the share of new appointments with technology backgrounds has increased from 12.1% to 15.5%, the share of new appointments with HR backgrounds has increased from 5.5% to 7.7%, and the share of new appointments with ESG backgrounds has increased from 2.7% to 4.4%.

A Majority of New Directors with Nontraditional Expertise are Female, Particularly for Directors with HR and ESG Backgrounds



Above is the percentage of new appointments in each nontraditional discipline who are women. Impressively, for every discipline aside from sales and legal in 2021, new nontraditional director appointments are majority women. The percentage of new technology appointments who are female has moved from 53% in 2019 to 62% in 2020 and back down to 58% in 2021. The percentage of new appointments with marketing experience who are female has actually decreased from 59% to 53% over the same time span, but still remains more than half.

By far the most illuminating breakdowns are in HR and ESG, where women represent the vast majority of new director appointments with those skillsets. For new director appointments with HR backgrounds, women accounted for 83% in 2019 and 72% in 2021. The proportion of new appointments with ESG backgrounds who are women has been steadily rising over the last two and a half years, skyrocketing from 64% to 84% female in 2021.

Commentary: Why Are These Trends Happening?

While the data we reviewed does not explain why there is an increase in skill set diversity on corporate boards, there are a few global trends that provide some possible explanations. Globally, but especially in both the US and Australia, scrutiny has increased for companies whose boards lack diversity. Companies are responding to this pressure in different ways, but the net impact is that boards are becoming more diverse in multiple ways.

What Is Happening with Board Diversity in the US, Australia and the UK?

In the US, companies are feeling pressure from governments, institutional investors, proxy advisors and asset holders alike – and they are seeing a sharp rise in issue awareness and social activism among their employees and local communities. In response, companies are interested to seek directors with diverse perspectives – both as a bulwark against risk, but also to shed light on potential business opportunities those from more traditional backgrounds might overlook.

In Australia, although the banking Royal Commission produced its final report in 2019, the new requirements are still creating ripples. Companies are more keenly focused on corporate culture, ethics and accountability across the board. In line with this trend, the Australia Institute of Corporate Directors (AICD) has issued guidance to corporate boards to strive for a minimum of 30% female directors and ensure the inclusion of indigenous and other ethnic minorities on their boards. These efforts are picking up momentum and Australia listed companies feel intense pressure to uphold these standards.

The UK is a bit behind the other two countries in terms of skill set diversity, but changes are likely on the horizon. We are likely to see an increase over the next three years for UK boards in terms of skill set, gender and ethnic diversity with the implementation of the targets set by The Parker Review last year. Beginning in 2021 with FTSE 100 companies and extending to all FTSE 250 boards by 2024, companies will be required to disclose their board's ethnicity and gender data, show they have 30% female directors and be required to have at least one ethnic minority.

Gender, Ethnicity and Skill Set Diversity Intersect

The global pressures on companies to increase the gender and ethnic diversity of their boards has, perhaps unintentionally, had an impact on director skill set diversity. Since so few women and ethnic minorities have held roles as CEOs, CFOs or COOs of major listed companies, as companies recruit and appoint women and ethnic minorities to their boards they are also onboarding directors from nontraditional professional backgrounds.

Further, there is a trend towards increasing diversity in the nontraditional backgrounds of female directors, which may point to boards becoming more inclusive, not just diverse. In the past, boards have responded to calls for increased gender diversity by looking to add female directors with backgrounds where women have historically held leadership positions, such as HR, Marketing and Legal. The trend towards a more diverse set of nontraditional backgrounds suggests that boards are widening the aperture of competencies that they look for in female directors. This, in turn, is an early indicator that boards are becoming more inclusive, acknowledging the value of diverse opinions, not just trying to meet diversity expectations.

Areas for Future Investigation

- Are trends in director appointments similar on a global scale?

- Given that nontraditional appointments are more likely to be women or ethnic minorities, is recruiting specifically for nontraditional backgrounds an effective avenue for increasing gender and ethnic diversity on boards?

- Where do we anticipate these trends will go? Will skill set diversity become a stronger focus area for regulators, investors, asset holders and other stakeholders – especially as pressure mounts for companies to have clear strategies on issues such as cyber risk and climate change?

Acknowledgements

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