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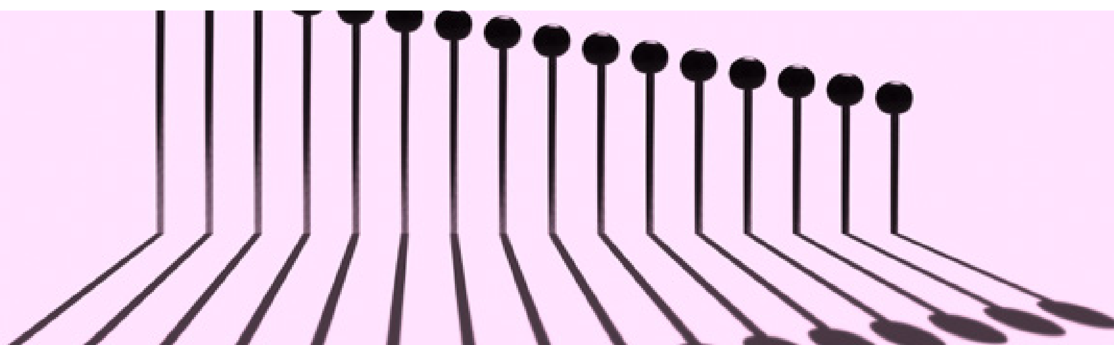

Nominating/Governance Committee in the Spotlight: Five Priorities for 2021

The days are gone when only members of the audit committee and compensation committee were in the hot seat. Today expectations of the nominating and governance committee are rising, and the spotlight on committee chairs and members is intensifying. Through our extensive work with nominating and governance committees of companies of all sizes, we have identified five key focus areas for the committee in 2021:

1

Optimizing board composition: The core work of the nominating and governance committee — board composition — has never been more important or more scrutinized, as investors increasingly announce plans to vote against the committee chair and members if boards are falling short on a variety of board composition metrics, including director tenure and diversity of gender, race and ethnicity.

But boardroom change frequently runs into the headwinds of slow turnover. And shareholders are increasingly concerned that boards aren't doing the necessary, and sometimes difficult, work to facilitate turnover. Surveys of directors support investor concerns. For example, 35 percent of S&P 500 nominating and governance committee chairs responding to a 2020 Spencer Stuart survey reported that their board had one or more underperforming directors in the past three years. And 49 percent of directors surveyed by PWC said a fellow director should be replaced.

Nominating and governance committees can no longer wait for directors to reach mandatory retirement age or volunteer to resign to evolve board composition. And director expectations that a board appointment is a guaranteed decade-plus role must change. Instead each director must understand that his/her appointment and re-nomination is based solely on boardroom needs and director performance. And this underpinning of tenure must be reinforced to every director each year.

Now more than ever, nominating and governance committees should:

- Thoughtfully develop a boardroom succession plan by determining the boardroom needs most relevant to the company's forward-looking strategies and risks and addressing composition vulnerabilities;
- Embrace a culture of continuous improvement by regularly evolving the board — at least every other year — to add new directors and fresh perspectives;
- Commit to leading when it comes to boardroom diversity of gender, race and ethnicity; and
- Promptly address director underperformance — by articulating expectations for improvement, seeking the director's resignation or determining to not re-nominate the director.

2

Enhancing board performance through board evaluations: Boards listed on the New York Stock Exchange have been required to complete an annual board evaluation for more than 15 years, and today most boards of companies listed on the Nasdaq Stock Market conduct an annual board evaluation. Investors expect these annual evaluations to be robust and constructive. The question for nominating and governance committees, which generally lead these reviews, is: Are our evaluations effective or are these rote, check-the-box exercises with limited value-add?

Since board evaluations are foundational not only to board effectiveness but also to optimizing board composition, nominating and governance committees should consider if and how the annual board evaluation can be enhanced by:

- Periodically (every two to three years) supplementing the annual board survey with director and key management interviews;
- Periodically (every two to three years) including peer evaluations as part of the board evaluation;
- Periodically (every two to three years) retaining an independent third-party — beyond outside legal counsel — to facilitate the board and peer assessments;
- Including time on the committee's agenda six months post-evaluation to assess progress on key takeaways and action items resulting from the evaluation; and
- Enhancing transparency to shareholders by providing summaries in the proxy statement on the evaluation process and high-level takeaways.

3

Overseeing environmental, social and governance (ESG) risks and opportunities: Today stakeholders — ranging from employees and customers to shareholders — expect companies to incorporate ESG factors into business strategies. No longer simply "feel good" issues, ESG considerations are now understood to be core to a company's long-term sustainability and value creation.

Investors are increasingly outspoken on ESG expectations. For example, BlackRock has called for uniform ESG disclosure standards and endorsed the approach recommended by Sustainability Accounting Standards Board (SASB). BlackRock also expects all public company boards to factor climate risk into their long-term strategic plans.

ESG oversight frequently is delegated to the nominating and governance committee. But ESG issues vary widely based on sector, industry and company culture, and one size doesn't fit all when it comes to best practices for overseeing ESG issues. As a result, nominating and governance committees should:

- Evaluate the company's key ESG risks and opportunities;
- Recognize that board oversight of ESG may be best handled by a variety of board committees and allocate oversight responsibilities as appropriate; and
- Ensure the company is communicating its ESG story and addressing the disclosure needs of key ESG rating entities, particularly since some investors are using ratings to shape their portfolios.

4

Determining if virtual-only board and committee meetings should continue in some form post-COVID: Directors now have one year of experience with all-virtual meetings of boards and committees. And while benefits of in-person meetings are missed, directors have realized that business can be handled efficiently and effectively via all-virtual meetings.

Board operations are a core responsibility of nominating and governance committees. As boards look ahead to a time when business travel and in-person meetings resume, nominating and governance committees should evaluate how to best leverage technology for board and committee meetings by:

- Determining if the number of in-person board and committee meetings should be reduced and supplemented by virtual meetings;
- Considering whether the sequencing of committee meetings should be changed. For example, rather than holding committee meetings immediately before board meetings, schedule virtual committee meetings on other days; and
- Evaluating whether the virtual meeting format creates opportunities to invite more outside experts to dialogue with the board.

5

Enhancing director onboarding programs: Effective onboarding continues to grow in importance as boards accelerate refreshment, add new directors who may not have experience serving on a board or reporting to a board, and meet virtually. As the committee responsible for overseeing director onboarding programs, nominating and governance committees should determine if enhancements to the induction program are appropriate. Spencer Stuart's Director Launch Pad includes an onboarding checklist that can be customized to be most relevant for each new director and for each company.

Conclusion

With investors increasingly scrutinizing the composition, diversity and quality of boardrooms, the spotlight is on the directors responsible for looking both inward and outward in order to evaluate the effectiveness of the board. In 2021, strategic nominating and governance committees will examine their board thoroughly, making changes, as appropriate, to address potential issues and enhance performance.

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