



THE VISIONARY BOARD AT WORK

DEVELOPING A CULTURE OF LEADERSHIP



WomenCorporateDirectors
A Foundation Inspiring Visionary Boards Worldwide

Pearl Meyer

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INTRODUCTION

Company success relies on both a robust business strategy and a strong, talented team to deliver it. Boards have long been deeply involved in working with senior management to assess, refine, and execute the company's business strategy. But what about the board's responsibility for leadership strategy? If business strategy defines *what* a company plans to do, then leadership strategy governs *how* a company will do it. Shouldn't an active board be equally concerned with both?

In 2016, the WomenCorporateDirectors Foundation (WCD) Thought Leadership Commission released its annual report *Seeing Far and Seeing Wide: Moving Toward a Visionary Board*. This year, the Thought Leadership Commission is building on that base to look at *The Visionary Board at Work: Developing a Culture of Leadership*.

While the board's responsibility for CEO succession is clear, we believe leadership

strategy goes much deeper. More than the mere identification of a collective group of current and future executives, it is the development and stewardship of a company's priorities and values—that is, its culture.

A recent global survey conducted by WomenCorporateDirectors and Pearl Meyer (subsequently referred to as the "WCD/Pearl Meyer survey") found that roughly 90 percent of respondents believe boards have a responsibility to oversee talent and leadership strategy—a finding that was consistent for US companies (92 percent) and multinational companies (88 percent) alike.¹ That said, in discussions among commissioners, there was a general consensus that "best practices" in this area are still evolving.

This anecdotal sense is further borne out by the WCD/Pearl Meyer survey, which found that despite nearly universal agreement that talent and leadership

strategy oversight is a responsibility of the board, just 11 percent of respondents feel boards are performing this duty well. Commissioners also agreed—and the global survey reiterated—that the board's role in overseeing a company's leadership strategy and culture were the same regardless of the country, industry, or company size or structure.

To further the dialogue on this topic, we've identified the following four areas for discussion:

Think Beyond the C-Suite: Develop Next-Generation Leaders

When it comes to leadership strategy, the board's first, *but not only*, responsibility is effective succession planning. Most boards view this as a primary role. But visionary boards think beyond the C-suite to actively identify and develop the company's next generation of leaders.

Nurture Culture at the Core: Create Firm-Wide Alignment and Engagement

Boards have numerous occasions to interact with senior management and create a shared view of goals and priorities. To realize a company's maximum potential, visionary boards seek opportunities to ensure that this shared view is present throughout the organization's culture.

Embrace the New Normal: Encourage Innovation

Reacting to change—both internal and external—has become par for the course in boardrooms. Visionary boards encourage management to proactively lean in to change as a way to create ongoing and future value for stakeholders.

Lead by Example: Self-Govern with Purpose

If the visionary board is pushing senior management to a stronger focus on leadership and culture, then it must be

willing to hold itself to the same high standards. A visionary board leads by example, demanding high performance and the strong engagement of its own directors.

A famous business maxim attributed to management guru Peter Drucker states that “culture eats strategy for breakfast.” If that is indeed true, then boards have a responsibility to understand and assess the health of a company's culture and leadership strategy as a critical component of the company's ability to deliver on its business strategy.

HOW IS LEADERSHIP DEFINED?

The concept of leadership should include the tangible qualities of the team assembled to run an organization—for example, their background, experience, skill sets, and demographics. It should also include that team's practices—how they as individuals and in groups collectively behave to develop and implement growth strategies, mitigate risks, manage crises, support employees, respond to customer needs, etc.

One of the primary responsibilities of the board is to hire and when necessary, replace the CEO. But the board's responsibility for talent and leadership development goes well beyond CEO succession planning.

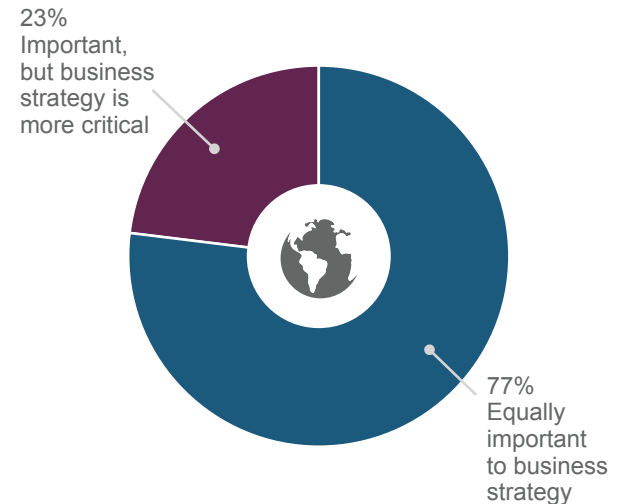
Boards have long understood this duty, and it is the area where boards are most likely to have policies and protocols in place. And yet, according to a report by Spencer Stuart, "CEO succession is inherently difficult. Very few boards excel at succession planning, yet investors and other stakeholders expect the board to have full command of the process. A seamless process is desirable but is not in itself a measure of success; boards can easily focus on process to the detriment of its principal purpose, which is to secure the very best available candidate."²

Visionary boards are both specific and detailed in their preparation for CEO succession, and they are thinking ahead by planning for other key positions

as well. They look beyond the current organizational structure to consider how changes in business strategy will broadly affect employee demographics and organizational needs.

Further, visionary boards look at leadership development from both a micro and a macro perspective. In addition to reviewing performance assessments for key high-potential individuals, visionary boards help the CEO consider the overall group dynamics of the management team. Today most boards assess their own combination of skills and expertise in some formalized manner. A similar approach can be used to ensure that the management team, in aggregate, has the experience and expertise necessary to successfully deliver on the company's business goals and objectives and that they are also nimble enough to respond to unforeseen changes and maximize emerging opportunities.

IN YOUR OPINION, HOW DOES TALENT AND/OR LEADERSHIP DEVELOPMENT FACTOR INTO A COMPANY'S OVERALL STRATEGY?



Source: WCD/Pearl Meyer Survey-Multinational Companies

Succession Planning

A typical process for succession planning involves the annual review of “ready-now” and “ready-soon” successors for all key senior positions. These debriefs generally include an overview of each executive’s position history and his or her most recent performance reviews. Obviously, an executed succession plan will create a ripple effect. Complete succession reviews also touch, at least briefly, on middle management bench strength to ensure that if someone is promoted into a C-suite position, there is appropriate backfill.

It’s essential for boards to pressure-test the viability of management’s succession plan; otherwise the annual succession review becomes a check-the-box exercise. While boards may not have enough familiarity with second- and third-level managers to probe senior management’s succession chart, they can provide important oversight to the process. For example, does the succession plan have



“There should be more discussion of diversity in developing leadership talent.”

Ann M. Veneman

the same individual listed as the sole successor for multiple positions? The flexibility of such “world-class athletes” is a valuable talent asset, but it’s appropriate to ask the CEO for scenario planning should that person be slotted into a new role and thus taken out of rotation for other positions.

Likewise, the board can also investigate the shelf life of current succession plans. Many plans have ready-now and ready-soon designations, but very few consider candidate “expiration dates.” For example, as ready-now executives near retirement, they will no longer be viable candidates for succession, or “expiration” may be self-generated the longer an individual remains in waiting.

In reality, a robust succession plan is two-tiered to include the following:

- A current succession plan that can be implemented immediately should a need arise, with ready-now candidates, their back-fills, and a plan of action for recruiting external hires where internal ready-now candidates don’t exist.
- A strategic succession plan—one that is expected to be executed at some point in the future and considers the anticipated term of current incumbents. This plan may eliminate some of the current ready-now candidates and focus more on the next generation of leaders who may be ready in two or more years.

The strategic succession plan works in concert with the company's evolving business strategy. Not surprisingly, companies often develop their succession plan with a focus on identifying internal candidates with the skills and experience to run the current business in the current organizational structure—this is really the

current “emergency” plan. An expected-succession plan also contemplates potential changes based on the company's long-term business and talent strategy.

WCD Commissioner C. Kim Goodwin noted, “One of my boards that exhibits best practices requires that we spend

three solid days each year talking about both leadership strategy and business strategy and making certain that those are connected because they really are intrinsically tied.”

Visionary boards ask whether anticipated changes in product mix or geographic footprint might alter

RETAINING TOP TALENT

The 2014 WCD Thought Leadership Commission addressed a number of critical issues often faced by compensation committees, including retention strategies. As the report noted, addressing these targeted, individual retention concerns is often a challenge for boards. Successful retention of high-potential ready-now executives often requires a multifaceted approach that goes beyond a simple retention bonus. Can we provide a rotational assignment or other growth opportunity? Can we pair the executive with a C-suite or board member mentor to help demonstrate the company's commitment? Have we communicated reasonable expectations about likely promotion timing?

The 2014 WCD commissioners developed a checklist for boards to consider in addressing retention concerns, including a few that are particularly relevant for ready-now executives:

- Conduct scenario analyses to understand the impact of retention awards on the overall leverage in the pay structure. While retention awards provide downside protection (i.e., they create a “floor” to expected compensation levels), they can also dampen upside leverage.
- Likewise, consider the impact at the time of the potential payout to avoid the unintended consequence of creating a secondary retention issue.
- Consider the retentive value of noncompensatory actions, especially for high-potential employees. Coveted assignments, expanded responsibilities, and board-level exposure can sometimes have more power than money.

expected roles and responsibilities, how any competitive landscape changes might affect business operations and staffing needs, or if changing workforce demographics might require a new organizational hierarchy. If the answers to these questions point to different succession candidates, then there is clearly a need for both short- and long-term succession planning.

Talent Assessment

Hand-in-hand with succession planning is a need to assess the organization's management talent. As a key component

of the succession review, the CEO should be prepared to discuss his or her assessment of each individual's strengths and weaknesses, as well as plans to address any developmental needs or opportunities through rotational assignments, individual coaching, and the like.

"Without time, energy, and resources spent on developing talent, you can't get to succession planning," said WCD Commissioner Arun Nayar. "Part of what I've looked for is rotation. How many different experiences are you giving your

executives so they're ready for the next higher level role?"

Visionary boards also have honest conversations about retention risks and mitigation strategies for ready-now candidates. After all, if you believe someone is ready for a promotion, chances are, at least one of your competitors agrees.

Likewise, if there are ready-now gaps in the succession plan, boards can be helpful in identifying external candidates. Senior management is usually very familiar with key executives at direct competitors, but

WHY BOARDS SHOULD CARE ABOUT LEADERSHIP DEVELOPMENT

The RBL Group conducted a survey of 430 portfolio managers on the factors they considered in making investment decisions.³ They were asked to divide 100 points based on the importance of three domains for investment decisions: performance, industry favorableness, and quality of leadership. As expected, investors clearly cared most about financial performance (38.6 percent), but it is noteworthy that the quality of leadership (28.4 percent) also had significant influence on investor decision-making. In fact, qualitative comments from survey respondents suggested that leadership quality would be weighted even more heavily, were it not for the difficulty investors have in assessing leadership quality.

the board's collective network casts a much wider net should the company need to recruit external hires.

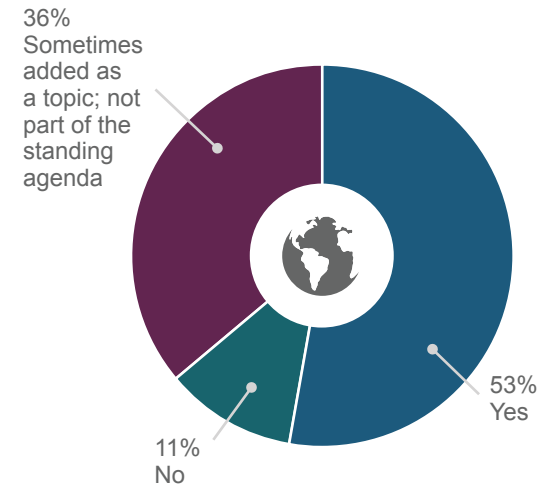
Beyond simply reviewing management's succession plans, visionary boards look for meaningful opportunities to get involved, to observe and interact with candidates for key C-suite positions in both formal presentations and informal gatherings. In addition to providing board members with chances to make their own assessments of current talent levels, these interactions create opportunities for board members to support the company's leadership development activities. WCD Commissioner Irene Chang Britt notes, "With the easy flow of talent these days in our relatively 'borderless' industries, it is more important than ever for boards to help their CEOs in talent attraction, development, and retention."

Leadership Development

The discussion of candidate readiness and talent assessment as part of the strategic succession plan naturally leads to questions about the company's approach to leadership development and the activities that support this growth. How deep is the bench, how full is the talent pipeline, and has the next generation of management been identified are important questions. But they may not be enough. Visionary boards also ask what's being done to support and accelerate the learning and experience curves of those individuals.

As with talent assessment, much of the activity around leadership development is created and executed by the senior management team. Similar to talent management and succession planning, though, the visionary board adds value

DOES THE BOARD AND/OR ANY OF ITS COMMITTEES HAVE STANDING AGENDA ITEMS RELATED TO COMPANY TALENT AND/OR LEADERSHIP DEVELOPMENT?



Source: WCD/Pearl Meyer Survey-Multinational Companies

through oversight. By asking questions about the process, such as do we do 360-degree reviews, do we offer executive coaching and external training opportunities, and how transparent is our career ladder, boards help management set challenging goals and monitor progress.

Over time, a robust leadership development program will deliver measurable results that the board can regularly track, such as an increase in ready-now candidates and internal promotions, higher retention of high-potential executives (and by extension other employees), and/or an increase in training programs offered and taken.

Several commissioners cited instances in which they and their fellow board members have been actively involved in the leadership development process



“Boards should monitor carefully that a culture of open, honest communication has been established.”

Izumi Kobayashi

throughout the year by partnering with leading succession candidates on joint projects or even volunteering to provide one-on-one mentoring of high-potential executives. In addition to this detailed involvement, boards can also help CEOs step back and assess their senior team on a macro level.

Commissioners agree that the assessment of individual talent is augmented by a high-level, comprehensive, and ongoing review of the overall team dynamics. WCD Commissioner Jan Babiak noted, “Some very important elements of succession

planning are to know what leadership characteristics we need and want and to make sure there is a cultural fit at all levels.”

In the same way that boards have begun to assess their own diversity and required skill sets, boards are also looking holistically at the composition of the company’s management team, and many board assessment techniques, such as a skills matrix, can be readily applied to management. Does management as a group and as individuals have the “just right” combination of skills, traits, and expertise necessary to successfully

deliver the company's unique business strategy? Have recent or anticipated changes in business strategy changed the skills and expertise required to succeed, and have those changes created any gaps in the current management group? Is the team appropriately diverse, and does it reflect the employee population and/or the company's customer base? Is there a mix of tenure among the management team? Has there been any strategic consideration of which positions are best suited to internal versus external candidates?

A full integration of leadership development, talent assessment, and succession planning is critical. In a paper published in the *Journal of Management Development*, Professor Kevin S. Groves of California State University presented a diagram depicting the interrelationships.⁴

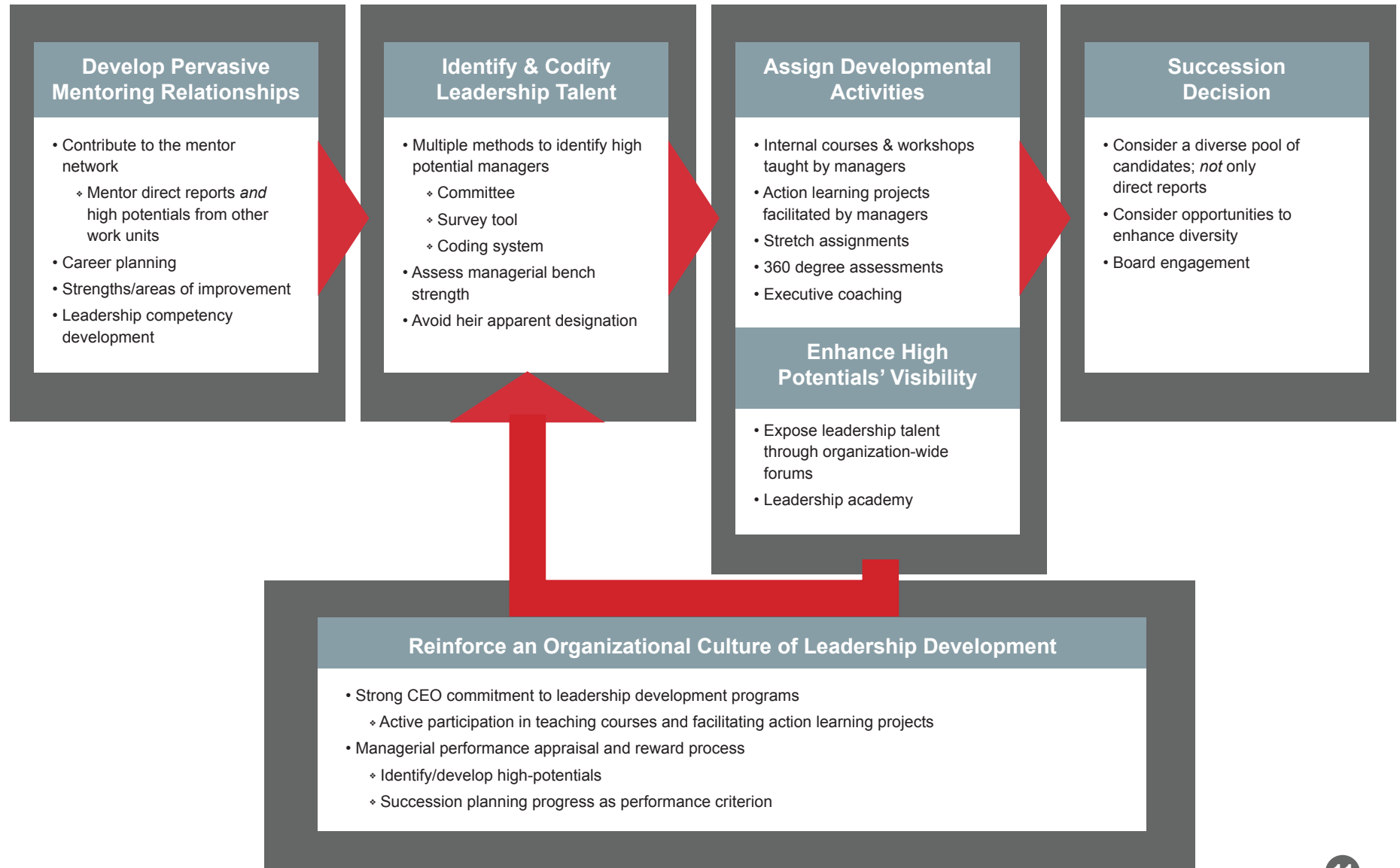
Granted, many of the items represent management activities, but ensuring that there is a robust, integrated process in place is an appropriate oversight role for the board. (See chart on next page.)

Boards that are expanding their oversight beyond the annual review of management's C-suite succession chart, engaging in discussions with senior management regarding talent assessment and leadership development, and offering their expertise and experience as mentors to the next generation of leaders are operating in a visionary manner. As covered in the next chapter, expanding the discussion of talent management naturally leads visionary boards to broader conversations about the company's overall culture and the board's role as monitors, if not stewards, of the company's mission, vision, and values.

Visionary Boards:

- Have both a current emergency succession plan and a forward-looking strategic succession plan
- Consider the changing talent needs implied by the company's long-term business strategy
- Actively address retention issues for ready-now candidates and have open conversations regarding their expiration dates
- Are active mentors to high-potential next-generation leaders
- Develop a skills matrix for the organization and consider team dynamics as part of the succession planning and leadership development process
- Fully integrate leadership development, talent assessment, and succession planning

An Integrated Leadership Development and Succession Planning Process⁴



It's undeniable that a thriving corporate culture can be the key to sustained competitive advantage. Culture has the power to drive innovation and growth, help weather disruption, attract customers, and engage employees. A positive culture can be infectious, and a negative culture disastrous. And while culture can be hard to define, when it's lacking, the results are alarming, as a recent Gallup⁵ poll shows:

- Only 22 percent of employees strongly agree that the leadership of their organization has a clear direction for the organization.
- Only 33 percent of employees define themselves as engaged.
- 51 percent are searching for new jobs or watching for openings.

The good news: Gallup's study also indicates that companies that have an engaged workforce report lower employee turnover, higher profitability, increased sales, improved safety, and enhanced quality control. Clearly, there is

a compelling and quantifiable benefit to a positive corporate culture.

As noted in the previous chapter, boards are increasingly involved in issues of talent management and leadership development. In the WCD/Pearl Meyer survey of global boards, 85 percent of directors indicated that they are receiving at least annual reports on these matters, and 90 percent indicated that they have a good sense of the talent profile and leadership skills of the senior management team. Although the vast majority of boards receive regular updates on the company's leadership development and also report understanding management's leadership skill set, one question remains: Why does cultivating an environment that results in high levels of employee engagement appear to be elusive?

Of the many issues to explore in answering that question, two are crucial: the board's ability to balance and align business strategy with the company's

culture, and its ability to truly understand the company's culture not just at the top of the house but at the core of the organization.

Business Strategy and Company Culture

Most boards are spending considerable time working with management to understand the triggers and pain points in the company's business strategy. Metrics are vetted, sensitivity analyses are conducted, and risks are explored.

An assumption often underlying this process is that the management team has the right skills and talent profile to execute on the goals. The WCD/Pearl Meyer survey data show that boards are presented with talent profiles and skills matrices, and it's through these assessments that the board is expected to determine whether management can deliver on the strategy. Unfortunately, these talent profiles and skills matrices rarely explore whether the management

team has the *cultural* traits that align with the realization of the business strategy. Additionally, they tend to be dry, focusing on how an individual fits in the succession plan but rarely delving into what makes the person “tick.”

WCD Commissioner Evelyn Dilsaver says, “You cannot execute your strategy unless you have a clear idea of what your culture is capable of doing. To me, culture is shorthand for, ‘How do decisions get made, and how do they get executed?’”

The fact is, there are significant elements of the culture that can help or hinder the business strategy and it can greatly benefit the board to understand the group’s—and each key individual’s—tolerance for risk, desire to innovate, appetite for growth, and adaptability. How do they manage through uncertainty and conflicts and balance autonomy and authority? What is their comfort level with accountability?

As noted, culture is difficult to define, and how it plays into the success or failure of a business strategy can also be nebulous. One illustrative example

is an organization at a crossroads with its traditional “cash cow” product lines in the early stages of decline, but its new products are still nascent. A management team with the appropriate balance of risk tolerance and adaptability is most likely to plot the right course, but a team that has shown tendencies to be inflexible or has shown—perhaps appropriately so in the past—a preference for maintaining the status quo during a time of crisis is not likely to do so. Certainly, the board can help execute, but that’s not a sustainable organizational structure. Visionary boards with an understanding of the cultural composition of the management team will have deeper insight into the viability of a given business strategy.

Consider another example. It’s very rare that a CEO presenting a performance assessment of his or her team will include an account of how gaps in leadership traits led to missed performance goals. However, without that candid assessment, boards don’t have complete information to discern if the performance miss was an operational or other business-based

MINDING THE GAP

How to understand the interplay between business strategy and culture:

- Conduct a culture and leadership diagnostic. Assess executive views on opportunities for career progression, risk tolerance, autonomy, accountability, and innovation. Include an assessment of an individual’s alignment with the overall mission, vision, and values of the organization to determine the degree of variability among the management team members.
- Map your current business strategy. Conduct a gap analysis between the results of the diagnostic and the company’s current business strategy. Results and implications may vary for different executive populations within the same organization.
- Prioritize the gaps. Review the gap analysis holistically, and determine the key areas that need to be addressed.

issue, or if it was a result of a cultural impediment. Boards with a more personal understanding of the individual members of the management team may be better able to zero in on the root cause of a performance issue.

Evaluating Tone at the Top

According to WCD Commissioner Arun Nayar, “The board has to keep an eye on how the culture is developing, and is that culture going to support the long-term sustainable growth of the enterprise.”

One way boards are currently facilitating their cultural understanding is by having different members of the management team present portions of the business strategy or plan that they are most closely associated with. While these presentations provide some tangible insight into the different members of the management team, they are also fairly scripted and thus may mask deeper individual leadership qualities.

Visionary boards are volunteering to partner with members of the management

team to fine-tune the business strategy and plans. The idea is not to have directors draft the business strategy and plan but, rather, to work with individual executives and ask probing questions that help properly vet the program and at the same time gain insights to their thinking and approach to the issues. This not only provides the board with a more intimate understanding of the strategy planning process but also affords significantly better personal understanding of the management team below the CEO and CFO.

This “partnering” concept, coupled with a request from the board to the CEO that performance assessment readouts include an assessment of values, alignment with culture, and leadership qualities, goes far to equip the board with a better understanding of their senior management team.

Continuing to engage in an open dialogue regarding the individual qualities and the culture of the management team

as a whole within the context of the company’s short- and long-term business strategy is key. Whether this happens annually or quarterly is dependent on the cadence that best aligns with the board’s own culture, but a thorough understanding of the management team’s culture is necessary to know if the company’s business strategy can be executed properly. Understanding the cultural pain points that could affect the strategy protects shareholder interests and guides the company forward in a way that exceeds what most companies are able to do.

Culture at the Core

It has also become increasingly important for boards to gain deeper insight into the culture and values that permeate the organization. On a global scale, from Volkswagen’s fraudulent emissions scores, to Takata’s faulty airbags, and Wells Fargo’s corporate malfeasance, it’s abundantly clear that once a culture is compromised, the impact is rarely limited to the executive ranks.

Former MIT professor Edgar Schein wrote, “Culture matters...If the organization begins to fail, this implies that elements of the culture have become dysfunctional and must change. Failure to understand culture and take it seriously can have disastrous consequences for an organization.”⁶ An engaged board cultivates the “tone at the top,” and at the same time “coaching the core” helps visionary boards safeguard shareholder value and protect stakeholder interests.

That said, it’s important to call out that *guiding* culture is distinct from *defining* culture and that culture cannot be defined in terms of “good” or “bad.” Rather, successful companies have the “right” culture—one that reflects the value of its stakeholders (including employees) and aligns to its business strategy. For every company that has a flat hierarchy, a high level of autonomy, and constant performance feedback, there are companies that thrive in the opposite environment. Boards intuitively



“How well people are managed, how happy and engaged individuals are—those are hard because they’re soft metrics, but it’s very important.” *Kapila K. Anand*

understand this, and visionary boards help management identify the gaps between company culture and business strategy and also hold management accountable for aligning with stakeholder interests.

These visionary directors are also stepping out of the boardroom to most effectively assess and guide the culture of the organization, and they are tapping into the company’s rank-and-file to function in their role with authenticity. WCD Commissioner Nina Henderson says, “In my experience, my contribution is optimized when an enterprise culture welcomes and enables director engagement beyond the boardroom. For me, the ability to gain insight through deep engagement is a key consideration in the decision to join a board.”

Typically this is done through site visits, rotating board meeting locations among offices, and attending corporate social gatherings. While all of these are absolutely worthwhile, they are typically orchestrated much like senior management presentations to the board. They are akin to attending Parents’ Day at a child’s school or camp—important to do because it provides insight and shows interest, but undertaken with the understanding that everyone is on their best behavior. WCD Commissioner Christine St.Clare says, “I don’t think you’ll get a real sense of a culture until you get out and you walk the hallways and you talk to the people.”

To further enhance the board’s understanding of the core corporate

culture, directors are beginning to “go behind the curtain” and attend trade shows and investor conferences to observe how employees are interacting with customers, competitors, and investors. Additionally, directors in B2C businesses (retail, hospitality, and to a lesser extent consumer products) are dropping in on store locations to observe day-to-day operations and interactions. These types of outings go a long way in helping directors align what they are hearing and exposed to at the top of the house with what is happening on the ground.

Visionary boards are also requesting that management provide more empirical data on organizational culture and employee engagement. Conducting engagement surveys on a periodic basis provides invaluable quantitative insight into whether the cultural values of the organization resonate with the employee base. However, it is not enough to collect

the data and track improvement on the company’s engagement score. Real cultural engagement requires infusing the lessons learned from the survey into a formal human capital strategy for the company, and for an effective leadership strategy to take hold, both management and the board need to participate in its formulation.

Especially powerful when combined with a demonstrated leadership development strategy, a holistic understanding of the company’s culture results in a greater ability to identify lapses and inconsistencies with the organization’s long-term objectives. Furthermore, it allows boards to more fully and authentically protect shareholder and stakeholder interests. It also sets the stage for an organization that’s much better equipped to tackle the shifts of a global marketplace.

Visionary Boards:

- Focus on understanding the level of employee engagement—both at the top of the house and at the core of the organization
- Coach culture through a deep understanding of the organization, its people, and the business strategy
- Encourage partnerships between board members and individual members of the management team
- Have frank conversations focused on understanding and dealing with any cultural imbalances of the management team
- Develop a higher level of accountability in managing the human capital risk factors through a strong human resource function and competency at the board level

A WELL-ROUNDED HUMAN CAPITAL STRATEGY

Although a human capital strategy should be organization-specific, an effective strategy accomplishes the following:

- Identifies cultural champions and empowers them to “coach the culture”
 - ◊ Finding individuals at all levels who embody the values of the organization and empowering them to proselytize those values through events, actions, and policies ensures a solid connection between the top and the core.
- Allows for more customization of compensation programs to better reflect the interplay between an organization’s business strategy and culture and an individual’s characteristics
 - ◊ Customization of compensation programs may be administratively complex, but if programs are not aligned with an individual’s values and the culture of the organization, he or she is weighed down by an effectiveness deficit right out of the gate.
- Encourages more collaborative goal setting
 - ◊ Individuals at work are more engaged when they are involved in determining the important drivers for the organization.
 - ◊ Many companies are comfortable doing this at the top of the house, but there are cultural benefits when it occurs in some form throughout the organization.
- Supports accountability at the top
 - ◊ A strong HR function, supported and guided by HR competency on the board, is essential to success.

CHAPTER THREE

EMBRACE THE NEW NORMAL: ENCOURAGE INNOVATION

The speed of change continues to accelerate, and so does a company's need to move with the times. A key output of a solid leadership strategy and healthy corporate culture is the cultivation of a management team and workforce that understands the importance of innovation and can deliver results.

In KPMG's *Now or Never: 2016 Global CEO Outlook*, Chairman John Veihmeyer notes, "We found that nearly half of CEOs expect their companies to be transformed into a significantly different entity within the next three years."⁷ The report also stated that 82 percent of CEOs are concerned about whether or not their current products and/or services will be relevant in three years.

Innovation and disruption are now standard business terms, and planning for innovation and predicting external disruption are becoming a regular part of the dialogue between senior management and the board. These conversations are often focused on growth strategies

and include thinking about, planning for, and adding new products, markets, or business lines. There may even be discussion of striving to disrupt an industry, all in an effort to drive long-term value. A small number of companies are going as far as to have divisions or subsidiaries focused on finding radical, market-changing innovation—Google and Alphabet are prime examples.

In spite of the increasing focus, actively managing innovation is not easy for boards or management teams. It's a complex notion composed of assumptions and facts, guesses and estimates. It's difficult for a board to know what questions to ask and when, and how hard they should press for answers. And change is typically difficult, which explains

why many companies continue to have a more traditional approach to thinking about growth, much less innovation.

The default position in assessing the competitive market is often defining strategy to react to current threats. Michael Beer, cofounder of the Center for Higher Ambition Leadership, said in an interview, "Social systems and organizational systems can stand in the way of being innovative." Yet forward-thinking boards are helping management anticipate where threats may emerge, while keeping focus on the company's own opportunities to create market change.

"As a board member and as an executive team, we have to recognize when the change is coming, what should



"The competitive review can't be insular; look outside the industry."

Pernille Lopez

we be doing now, and how should we be investing to recognize that change is going to affect our entire organization,” notes Evelyn Dilsaver, WCD commissioner.

Today, board members are doing many of the right things: staying current in their business and industry, holding discussions with the management team about the business strategy, and challenging the status quo. They are seeking to understand if the management team is appropriately receptive to thinking differently, rather than relying on the company’s historical perspectives to drive innovation.

Innovation Governance

According to an article from Ross Dawson, founding chairman of the Advanced Human Technologies Group, “Governance—in establishing structures and processes that define accountability and mitigate risk—is the domain of the board of directors. Yet the inherent risk aversion of traditional corporate governance structures has a real potential

to quash innovation, in turn possibly risking the very future of the organisation. It is the responsibility of the board to establish governance structures that balance risk and potential benefits, and also consider the very high organisational risk of not undertaking innovation.”⁸

Recognizing this, visionary boards are considering their own form of “innovation governance” through which innovation is considered as it relates to strategy review; audit, risk, and performance assessment; and talent, leadership, culture, and remuneration.⁹

Taking a holistic governance approach to innovation means that each committee and the full board take an active role in directing this process with management. Of course, it also means adding more responsibilities and time requirements to current roles in order to do this well. As a result, focus on these issues may also provide an opportunity for boards to reconsider how and where time and resources are spent on tactical versus strategic topics.

Strategy Review

Most boards and management teams conduct an annual review of the business strategy, yet many do not have innovation as an agenda item at their board meetings, suggesting substantial room for growth and opportunity. According to one director quoted in the KPMG report *Innovation, Disruption, and the Role of the Board*, “Innovation ought to be a part of every board discussion. It’s not something you do once a year, or even just at regular intervals like once a quarter. It’s an ongoing board conversation that needs to occur.”¹⁰

A challenge to being a good steward of innovation is that some directors may have limited experience in this area, especially as it relates to technology. Visionary boards combat this by conducting ongoing educational sessions on industry and technology trends. They augment their experience with presentations by topical specialists, industry analysts, institutional

shareholders, customer panels, investment bankers, or generational experts.

One interesting visionary board example shared by a WCD commissioner involves pairing individual directors with rotating management team members to co-lead a discussion of a specific topic on innovation and strategy at each meeting. This allows more individuals to get involved in presenting to and leading discussions with the board, and it allows directors and the management team to learn from and get to know one another.

A handful of leading companies have even created an innovation committee of the board. A great example of synergy between strategy review and committee development is highlighted in a white paper from the Center for Higher Ambition Leadership describing how the medical technology company Becton Dickinson instituted a science, marketing, innovation, and technology committee.¹¹ The goal

was to help address innovation and grow the business with new products and practices. Director and committee chair Dr. Al Sommer is quoted in the report, “We challenged management to understand their track record of innovation, and management rose to the task. They became their own best critics, introduced processes to drive innovation and a culture of challenge.”

Visionary boards can also more generally support management’s innovation initiatives by affording the time and space to “play,” to be creative, to be uncomfortable, and to fail. True support for this approach goes further to include allocating resources and establishing a budget that puts real teeth into a successful innovation program.

Audit, Risk Assessment, and Performance Review

In the areas of cost and risk, boards generally guide management through evaluation—asking questions about programs, assessing and auditing results, and helping establish reasonable risk tolerance levels.

No doubt risk is an inherent part of being an innovator, just as risk is an inherent part of a company’s business strategy. Visionary boards are including innovation practices—and the potential to be disrupted—in the board’s regular evaluation of risk assessment. The board can further help to oversee this risk with the management team by establishing funding practices related to innovation and, according to WCD Commissioner



“A technology [or innovation] committee should be strategic and opportunistic, not just defensive or risk based.”

Phyllis J. Campbell

Elaine Eisenman, “defining acceptable levels of loss in the service of opportunity.”

In tracking and reviewing innovation performance, one forward-thinking approach is to ask management for a scorecard that sources, identifies, and

tracks innovation activities throughout the organization. This scorecard captures the entire innovation life cycle, and it includes elements like idea generation, technical and market research, funding and operational cost estimates, risk

assessment, go/no go decision points, and anticipated revenue. Innovation scorecards can provide the board a high-level overview of incoming ideas, progress, allocated resources, and projected reach, impact, and return.

Ideas for Managing an Innovation Program

The Idea Tank

Select one board meeting a year (or add a meeting) to use the boardroom as an idea tank for board members to hear pitches on new and different ideas to help grow the company.

- Ideas are presented by the employee teams that came up with the idea and developed the pitch.
- The winning pitch receives funding to pursue further development of the new idea.
- This exercise is an opportunity for leadership development, and it provides employees with exposure to the board and vice versa.
- This exercise also facilitates the board's support of a culture of innovation by providing funding and endorsement of an idea and allowing for creativity.

Acting as an Activist

Select one director at each board meeting on a rotating basis to serve as the “acting activist”—the person tasked with asking the difficult questions and challenging management and the board to think through all of the issues.

- Each director will serve in this role, and establishing ground rules for performing this job well, and with respect and dignity, are key to success.
- This practice allows for the tough questions to be asked without any one individual director being judged for asking too many questions.
- This practice may take the pressure off other directors, but it should not replace the need for other directors to speak up as well.

They are useful tools to assist the full board or any of its committees in evaluating and auditing results and pinpointing areas for change and improvement.

Talent, Leadership, Culture, and Remuneration

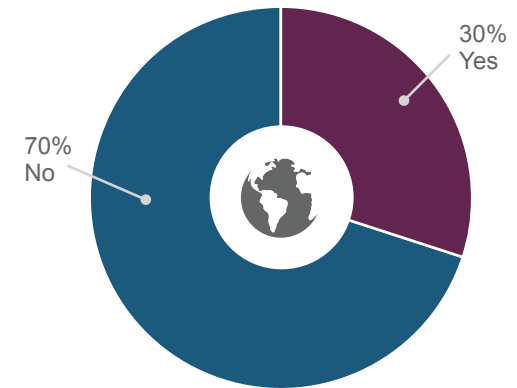
Perhaps most critical to facilitating an innovative organization is managing the right talent, leadership, culture, and compensation programs.

One of the primary roles of the board is CEO selection, as noted earlier. But how many boards are including innovation and/or technology proficiency in their CEO selection criteria or looking further down the ranks of management and considering succession candidates in the context of their approach to innovation? Visionary boards are incorporating this into formal leadership development processes and talent evaluations.

The selection of an innovation-focused CEO and the development of a supporting management team has a tremendous impact on whether or not the corporate culture supports or suppresses innovation. Building an environment where employees can promote creative thinking and fail without negative ramifications is key.

Visionary boards are also signaling the importance of innovation by including performance goals in their compensation programs. Innovation-focused performance metrics and their corresponding weightings can be in the form of either leading (strategic) or lagging (results-focused) metrics and they can be

ARE THERE ANY COMPENSATION INCENTIVES FOR THE MANAGEMENT TEAM RELATED TO COMPANY TALENT AND/OR LEADERSHIP DEVELOPMENT?



Source: WCD/Pearl Meyer Survey



“In this age of innovation and fierce competition, does our culture support and vet new ideas in a way that can take those ideas to a meaningful result?” *Kathleen Mason*

in the short- and/or long-term incentive plans depending on the appropriate time frame for the objectives.

As with any high-priority initiative, it's important for companies to explicitly announce their intentions around

innovation programs and their place in the business strategy. This communication, if done well and reinforced frequently, can greatly help in fostering an organization-wide culture of innovation.

Examples of Metrics that Guide and Assess

Leading Strategic Performance Metrics

- Evaluation and qualifying process for new innovative ideas
- Moving ideas through the scorecard
- Go/no go determinations
- Technology investments
- Other milestone-based metrics

Lagging Performance Metrics

- Percent of sales from new products and/or markets
- Research and development spend
- Employee turnover
- Employee engagement and satisfaction survey results
- Impact on the organization

Visionary Boards:

- Determine if innovation governance oversight is a full board or committee activity
- Support play, creativity, and failure in the company culture appropriately
- Ask management to develop a scorecard that outlines the important stages of innovation to review with the board regularly
- Provide proper funding, resource allocation, and identification of talent and technology needs
- Establish “acceptable loss” levels and include innovation evaluation in the board’s regular risk assessment
- Establish talent selection and performance evaluation innovation criteria, and include innovation milestones and goals in compensation programs

Although the board has a number of critical responsibilities, one of the most sacred is the responsibility to self-govern. As the body charged with balancing shareholder and other key stakeholder interests with the long-term interests of the company, navigating the self-governance responsibility is fundamental to delivering effective corporate governance. In that regard, all stakeholders rightly expect boards to hold themselves to the highest standards given that boards essentially have the ability to select, evaluate, and compensate themselves. The key to delivering on this standard is an understanding of the processes and practices that propel a board from being compliance focused to one that's more focused on value creation.

As a first step in unlocking corporate value, boards often discuss the importance of setting the right tone at the top. This outlook manifests itself in the strategy that the company adopts, the degree of risk the company is willing to tolerate, and the level of company performance that's expected.

Yet in this age of heightened accountability, the top is not limited to the CEO and his or her management team. It also includes the board itself. WCD Commissioner Eileen Fusco says, "The board needs to have its own leadership strategy, compatible with the company's and senior management's. We are where the buck stops. If we're not leading by example, then we're not doing one important aspect of our job as the board."

Possessing shared values and similar behaviors facilitate a board's ability to lead by example effectively. Interviews with WCD commissioners across the globe indicated strong support for colleagues who exhibited:

- A desire to build a governance structure around the mission of the organization rather than focusing on prevailing practices
- An ability to work constructively by asking probing questions and challenging management when appropriate

- The capacity for catalytic learning—to absorb new ideas quickly and translate them into actionable outcomes
- Independent-mindedness
- A focus on transparency

A forthcoming report from Spencer Stuart¹² offers additional ideal director attributes including:

- Fair minded, having absolute integrity and wisdom, and above all courage and common sense
- Internationally minded and multilingual
- A relationship-builder and an ambassador
- Articulate and persuasive while being a good listener and a good communicator
- Low in ego yet high in self-confidence

This input suggests there is a shared culture of board leadership that transcends country, industry, company size, and structure—a global board leadership mindset.

It also suggests that although board culture can be aligned with corporate culture, it should not replicate it. Viewing the board as an exact extension of the company isn't reasonable or appropriate. Visionary boards strive to create a cohesive social unit that appropriately stands apart from the company. Unlike corporate culture that reflects the shared values of a singular entity, board culture is more directed because of the board's unique position of accountability to a variety of stakeholders.

Expanding the Board's Self-Awareness: Going from Good to Great

In recent years, boards have made considerable strides in formalizing their processes to ensure that decision-making happens in the context of good governance. The focus to date has been on the board's authority and how it functions. The next stage in the board's evolution is to concentrate on how the board members interact among



“The board needs to work together in a harmonious and effective manner. How the board works is a mirror of how the management team is expected to work together.” Jyoti Narang

themselves and with management, and how those interactions influence decision-making.

The most prominent assessment of how the board performs and interacts within itself is the board evaluation, which typically focuses on how the board and its committees function as a whole and assesses the individuals in board leadership roles. WCD Commissioner Phyllis J. Campbell says, “Self-evaluations should go beyond generic tablestakes assessments and review value-added traits like critical thinking and intellectual curiosity.” While insightful, most evaluations in their current form are also limiting because they do not solicit feedback from the board's key constituents: management and shareholders.

Visionary boards are adopting a board assessment system that includes a 360-degree feedback loop and facilitates the incorporation of valuable insights from members of management that they work with. Soliciting feedback from shareholders is trickier, but it can also be instrumental in evaluating board effectiveness. While shareholders can express their approval of individual directors through annual reelection votes, it's a blunt instrument used to deal more with problems than advancing solutions. As a normal course of regular business, many boards are adopting formal annual outreach campaigns with shareholders to discuss company strategy and compensation programs. At the same time, some visionary boards also solicit feedback on overall

corporate governance matters and more specifically, the shareholders' view on the board's effectiveness. This level of communication may also have an added effect of confirming robust board processes, providing further confidence to shareholders.

An action plan to process this information is essential. One implementation strategy is building on the skills matrix many boards have already adopted and creating profiles for each director that identify both strengths and weaknesses. This can show current gaps and inform future learning opportunities and recruitment efforts. Boards can use these individual profiles to engage directors in continuous learning that includes both hard skills like industry deep dives, financial training, or regulatory updates and soft skills like meeting facilitation and consensus building.

This greater understanding of the values each director brings to the table through the addition of a culture



“As directors, we need to understand the future by bringing in experts to educate the board and management.”

Lady Barbara Judge CBE

and values assessment allows for even more transparency and a more rigorous strategic planning process as the comprehensive matrix is mapped to the company's business strategy. This integrated analysis can then identify any gaps or areas where the board may improve its management oversight through training or refreshment.

Getting Composition Right

Evaluating the board across a skills, culture, and values paradigm is one critical aspect of assessing effectiveness, but another vital component is the board's own composition, including its diversity and refreshment.

Although boards today are highly

attuned to addressing their own diversity, the organizations they represent are experiencing varying degrees of success, partly due to the narrow use of the definition of diversity. Visionary boards are starting to internalize a new definition of diversity that goes beyond race and gender to more broadly include characteristics like cultural experience, socioeconomic background, specialized expertise, and age, and it may also include representation from a company's end market or customer base.

WCD Commissioner Catherine Allen explains, “When you look at board composition, first you may look at male, female, or race. The most important factors are those more elusive things,

such as how you were brought up, your political leanings, whether you use inductive or deductive reasoning, the experiences that you've had. It's important to have this type of diversity. The most successful boards have this culture of inclusiveness."

Just as a check-box approach to diversity is giving way, it's no longer enough to ask if a board should be refreshed. The better questions now are when and how refreshment will occur. Although the market sometimes rewards tenured boards with a "stability premium," a recent QMA research study of 3,000 companies spanning 18 years indicated that "After 9 years, the positive relationship between tenure and company value reverses and values decline, especially at fast-growing companies that require directors to keep up with technological trends."¹³

The fact is despite the multitude of excellent reasons associated with a

director stepping down from a board, it continues to be met with an assumed cloud of nonperformance—a stigma that should change. Having an explicitly defined refreshment approach can help greatly and may incorporate one of the following:

- A formal structure with term limits or mandatory retirement ages
- A semiformal structure that manages the gaps and/or excesses based on the determination of the board's skills and culture matrix, and takes the necessary steps to add or remove directors appropriately
- No structure where refreshment is ad hoc and dependent on the nominating and governance committee and/or the lead director or non-executive chair taking action when necessary

Together, the board may collectively determine which of the approaches aligns with its culture and the needs of the

organization, and it is helpful to broadly communicate this defined practice.

The Time Trap—Sacrificing Value for Compliance

Similar to any group or team dynamic, no matter how great the individual members are, they must come together to execute on their directives. With so many compliance issues to address, it's a real challenge for boards to spend enough time being stewards of shareholder value creation. WCD Commissioner Kathleen Mason says, "Committee meetings and reports to the board too often leave little time to discuss where we are in our strategic direction and with our leadership team."

As noted in the previous chapter on innovation, reallocating the time boards spend on compliance versus strategic issues is a valid challenge to take on. Visionary boards are examining ways to change how they work—including the

use of technology—to more quickly clear through the compliance responsibilities and focus on strategy.

Some visionary boards are starting to question the standard committee structure and asking questions such as these: Is there better synergy by creating a people committee that can cover the responsibilities of both nominating and governance and compensation, with an added focus on leadership development? Could the charters of the finance, audit, and/or risk committees be consolidated? Would the implementation of a strategy committee effectively assess innovation and disruption? Would allowing all board members to attend all committee meetings, independent of their committee membership, reduce or eliminate the need for reports and therefore create more time



“Show me your agenda and I’ll show you your priorities.”

Michele J. Hooper

for full board meeting discussions?

These visionary ideas can facilitate more focused time spent on evaluating strategic decisions, doing so through the prism of an extended time perspective (i.e., five or more years), and playing that often-mentioned role of “internal activist.” After all, spending more quality time on understanding future sources of growth and asking probing questions on strategy, financial performance and forecasts, and compensation programs are the real issues at hand and the factors that ultimately lead to value creation.

Visionary Boards:

- Prepare an overall board skills and culture matrix and conduct a gap analysis to identify the skills and values that support the company’s business strategy
- Construct a profile for an ideal board candidate and share with current directors
- Initiate discussions on board governance with shareholders as part of regular outreach efforts
- Focus attention on identifying a pipeline of rising director talent within the industry or desired knowledge area to “keep an eye on” potential recruits
- Consider restructuring the roles and responsibilities of committees to reallocate time more toward strategic discussions
- Have a documented policy regarding board refreshment

HOW DOES THE BOARD APPROACH ITS OWN LEADERSHIP AND TALENT DEVELOPMENT?

Generally do not address the topic



Informal discussions



Formal guidelines



Regular self-evaluations

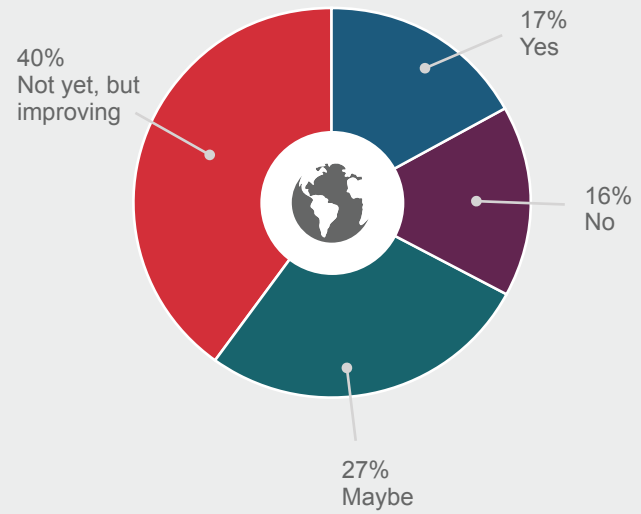


Outside or third-party evaluations



Source: WCD/Pearl Meyer Survey

DO YOU FEEL THE BOARD IS A LEADING EXAMPLE FOR OTHER BOARDS IN TERMS OF ITS OWN TALENT AND/OR LEADERSHIP DEVELOPMENT?



Source: WCD/Pearl Meyer Survey

IN CONCLUSION

Our commissioners shared many visionary practices related to the board and its stewardship of leadership and culture. Yet questions remain about the effectiveness of boards in this expanding area of responsibility and oversight.

The WCD/Pearl Meyer survey uncovered a clear dichotomy between what leading boards agree they should be doing and what is happening broadly in boardrooms today. Ninety percent of survey respondents said the board has responsibility for overseeing or guiding a company's talent and leadership strategy. However, when asked if guiding a company's talent and leadership strategy is something that most boards do well, 89 percent said "no."

This report shares ideas meant to inspire dialogue and continue discussion in boardrooms that can help bridge the gap between intention and execution.

What are the Key Takeaways?

The reality is there's a culture—however defined—at the core of any company, and it bears much responsibility for the success or failure of the organization. Similarly, the culture of the board is central to its own effectiveness.

As commissioners discussed various issues of global business culture and leadership in preparing this report, we continually uncovered four central themes common to the visionary boards who are creating an effective balance between

business and leadership strategy:

- Develop talent and the next generation of leaders below the C-suite.
- Understand that corporate culture goes deeper than the first level of management and know the importance of there being core values that are shared throughout the organization.
- Anticipate change and believe encouraging and embracing innovation is central to the organization's growth.
- Lead by example.

Among the most visionary directors and business leaders, we find there is a sense of commonality and shared purpose—an understanding that people and culture are the key to unlocking value.

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Go to www.pearlmeyer.com/2017WCDThoughtLeadershipReport or visit www.womencorporatedirectors.org.

Thought-Starter Questions for Visionary Board Discussions

Leadership Strategy

- How realistic is our succession plan; does it look different if we fast forward two to five years?
- How do we identify high potential executives and next-generation leaders? What development programs do we have for them?
- Have we developed an inventory of skills, traits, and expertise necessary for our business strategy and do we know how the current management team maps against that list?
- How do we measure progress and success?
- Can we create accountability for senior management through compensation?

Corporate Culture

- Does the company's culture support the current business strategy?
- How involved should we be in coaching culture?

- How does the company assess executive and employee engagement and how is that information used?
- How does management handle top performers who don't represent the company's culture or embody its values?
- Do we have the right level of human resource competency on our board?

Innovation and Growth

- Who can disrupt us and how, and can we impose disruption and how?
- How does the company facilitate idea generation?
- How does the management team take in and assess new ideas?
- Should we be hearing more about internally generated ideas and can we serve a role in the creative process?
- Does our culture support an environment of creativity, as well as failure, without negative ramifications?

- How can we use our compensation programs to help drive behavior around innovation?

Self-Governance

- What is our own culture and does it support the company's business strategy?
- Should our evaluation process include feedback from key stakeholders?
- Do we need a mechanism to help identify gaps in our experience and skill sets?
- Should we periodically assess our structure and policies, including refreshment, as they align with stakeholder goals?
- Should we consider any alternative board compensation structures that might promote leadership?
- How do we define diversity?

2017 WCD THOUGHT LEADERSHIP COMMISSIONERS

Our distinguished group of commissioners includes highly accomplished directors, many of whom have more than 20 years' experience in the boardroom. Their contributions to this report are based on expert insight from a diverse set of business environments, including consumer goods, energy, entertainment, finance, healthcare, hospitality, information technology, life sciences, pharmaceuticals,

professional services, retail, and transportation.

Beyond representing numerous Fortune 500 companies headquartered in the U.S., they also serve on more than 33 global and multinational boards, including those with headquarters in Australia, Canada, Germany, India, Ireland, Japan, Luxembourg, Malaysia, the Netherlands, Switzerland, and the United Kingdom.

Collectively, these companies are operating on every major continent in more than 120 countries.

Their perspectives have guided the direction of this report and we thank them for their time and commitment to the exploration of corporate leadership and culture.



Catherine Allen



Kapila K. Anand



Zarinah Anwar



Jan Babiak



Irene Chang Britt



Phyllis J. Campbell



Julie Hembrook Daum



Evelyn Dilsaver



Elaine Eisenman



Eileen Fusco



C. Kim Goodwin



Kathy Hopinkah Hannan



Nina Henderson



Michele J. Hooper



Lady Barbara Judge CBE



Izumi Kobayashi



Jannice Koors



Elaine La Roche



Pernille Lopez



Kathleen Mason



Melissa Means



Jyoti Narang



Arun Nayar



Jana Schreuder



Aalap Shah



Susan S. Stautberg



Christine St.Clare



Ann M. Veneman

ABOUT THE WOMENCORPORATEDIRECTORS FOUNDATION

The WomenCorporateDirectors Education and Development Foundation, Inc. (WCD) is the only global membership organization and community of women corporate directors. A 501(c)(3) not-for-profit organization, WCD has 76 chapters around the world. The aggregate market capitalization of public companies on whose boards WCD members serve is over \$8 trillion. Eighty-five percent of WCD members serve on a public, private, or family business board.

Our Mission

WCD seeks to inspire visionary boards worldwide by providing education and tools that keep members engaged, informed, and high performing as directors. WCD also advocates for increased representation of women on boards and in board leadership positions. Through our global network, WCD provides governance training sessions and shares notices of open board positions to increase the pipeline of qualified female board candidates.

For More Information

To learn about the benefits of WCD membership and how to join, visit www.womencorporatedirectors.org.

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Contact the Authors

In 2014 Pearl Meyer chaired the inaugural WCD Thought Leadership Commission report. We are pleased once again to lead the discussion of key boardroom issues on behalf of directors worldwide and the organizations they serve. The report authors welcome and encourage further conversation on the topics examined in this year's report. Contact:

Jannice Koors, managing director: jannice.koors@pearlmeyer.com or (312) 242-3052

Melissa Means, managing director: melissa.means@pearlmeyer.com or (508) 630-1487

Aalap Shah, managing director: aalap.shah@pearlmeyer.com or (212) 407-9511

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NOTES

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