A deeper dive into talent management: the new board imperative

As companies grapple with social concerns like employee diversity and inclusion and income equality, they are also facing business transformations. Talent management is critical—and so is director oversight.

September 2020

Corporate directors have traditionally focused their talent management efforts on the C-suite, leaving oversight of the broader workforce to senior executives. But talent shortages, pressure from investors and other stakeholders to address social risks, and the astonishing pace of business and digital change have made it critical for boards to provide greater oversight of talent management at multiple levels of the organization.
Rethinking talent

Providing oversight of a company’s top talent has long been a core responsibility of corporate boards. They play a critical role in the hiring and firing of the CEO, evaluate the performance of top executives, develop leadership succession plans and ensure their companies have a robust pipeline of talent to execute company strategy.

Traditionally, directors have focused their talent management efforts on the C-suite, leaving oversight of the broader workforce to senior executives. But many boards have come to understand that a strategy is only as good as a company’s ability to execute it. And strong execution requires talented people at all levels of the organization—particularly when most companies are reinventing themselves to contend with disruption and technological advancements.

These days, the ability to attract, develop and retain the best talent has become a critical business differentiator. Yet it is a challenge. In a recent survey, CEOs cited the low availability of key skills as one of the top threats to business in 2020.1 As widespread transformation continues to drive demand for workers with new skills, not having a comprehensive plan for acquiring and developing these workers can hurt a company’s ability to grow and innovate. As a result, boards must play a larger role in ensuring their organizations have the talent they need to execute new strategies.

Social issues that impact talent management are getting more attention—some as a result of the COVID-19 pandemic and some that existed before it. These issues represent key risks for investors and are top of mind for a much broader stakeholder group: access to job opportunities, diversity and inclusion, and income inequality, to name a few.
Rising investor pressure

Long before the COVID-19 pandemic, institutional investors began paying closer attention to talent management, and some more recently communicated specific expectations for public companies related to diversity and inclusion (D&I). In support of these priorities, they are urging boards to become more involved in workforce planning and development.

Many investors believe that in order to understand the forces shaping their business, companies need to take action on D&I issues. They are looking to companies to promote D&I principles within their operations. Investors also believe that D&I is associated with increased workforce productivity, reduced turnover, and higher customer satisfaction.²

In August 2020, State Street Global Advisors sent a letter to board chairs stating that starting in 2021, it will ask companies in its investment portfolio to make specific disclosure available to shareholders related to their racial and ethnic diversity, including their: (1) strategy; (2) goals; (3) metrics; (4) board composition; and (5) board oversight related to D&I.³

The California State Teachers’ Retirement System (CalSTRS) also emphasizes the importance of the board’s role in raising the bar for human capital management, “the most important asset of any organization.” Their corporate governance principles further state that, “boards should have an active role in setting the company culture and oversight over the company’s approach to human capital management, which should include: commitment to diversity and inclusion; gender equality; employee development.”⁴
The SEC agrees that investors would benefit from enhanced disclosures in this area, and therefore in August 2020, the SEC amended its human capital disclosure requirements. Under the new rules, companies will be required to provide a description of their human capital resources, including any human capital measures/objectives that the company focuses on in managing its business (e.g., those that address the development, attraction, and retention of personnel).\(^5\)

Amid this rising investor and stakeholder pressure, directors are taking a hard look at talent management at their companies. And they see room for improvement. Nearly half of the directors in PwC’s 2019 Annual Corporate Directors Survey say their companies are doing a “poor” or only “fair” job of developing a diverse pool of executive talent. Roughly one-third say they are missing the mark on recruiting a diverse workforce and one-quarter say the same about addressing gender-related pay differences.\(^6\) These are important issues given the research showing that diversity in the workforce leads to greater innovation, better decision making, and stronger company performance.\(^7\)

### Needs improvement

Directors say management needs to do a better job of:

- Developing diverse executive talent
- Recruiting a diverse workforce
- Recognizing and addressing gender pay disparity

Three steps to broader board oversight

Taking on a more substantive talent management oversight role isn’t easy. It requires boards to strike a balance between acting strategically to ensure the strength of the company without stepping into the role of management. To maintain a healthy balance, here’s what directors should focus on at three levels of an organization:

1. **The C-suite.** Directors are responsible for selecting and monitoring the performance of the CEO. As part of that responsibility, the board needs to hold the CEO and other C-level executives accountable for company performance on talent management. This has become even more important as CEO tenure has fallen to a median of five years, down from six years in 2013. As tenures get shorter, CEOs are under more pressure to deliver short-term results. Tackling longer-term initiatives such as upskilling the workforce and increasing diversity become even more challenging. So, boards must demand that talent development remains a top management priority despite the pressure to meet shorter-term performance targets.

They can do this by requiring top executives to:

- Achieve strategic talent management objectives
- Uphold healthy and ethical corporate values to set the right tone at the top
- Model desired workplace behaviors
- Create a diverse and inclusive culture

2. **Up-and-comers.** Boards need to ensure the company has a strong talent pipeline for all C-suite functions. They can do this by using a “C-Suite Readiness Chart” (refer to chart on pg. 6) that identifies senior executives who could assume those positions now, as well as in one to five years in the future. In the meantime, they should take steps to get to know and assess the capabilities of these high performers by:

- Having them present to the board on major initiatives
- Assigning them to work on special board projects
- Inviting them to board dinners and other social events
3. Middle management. Getting to know middle managers is particularly difficult for board members. At this level, the board can provide oversight by gaining an understanding of the organization’s talent philosophy, culture and talent needs for the future. This includes:

- Reviewing talent retention strategies and compensation programs to ensure they address issues like gender equity and diversity and inclusion
- Reviewing metrics that indicate whether the culture aligns with company strategy
- Asking how management plans to address current and future skills gaps created by the adoption of artificial intelligence, machine learning, big data, advanced analytics, cloud technology and automation

Sample C-Suite readiness chart

Chief Financial Officer

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Board oversight in action

Board efforts to ensure a company’s talent management approach aligns with corporate strategy are best supported by three tools:

1. Data. In today’s data-driven world, understanding and monitoring key metrics can help board members spot warning signs and make better informed decisions. A review of talent management-related key performance indicators (KPIs) can identify red flags and opportunities for improvement. Helpful data points include:

   - High turnover and high-performer departure rates
   - Unfavorable exit interviews (particularly those of high-performing employees)
   - Positions that remain unfilled for long periods
   - Succession plan success (number of times a plan has been established, but management ultimately hires someone else)
   - Low employee engagement scores (including an analysis of scores by diverse groups)
   - Lack of progress on diversity and inclusion efforts
   - Whistleblower complaints and lawsuits involving HR issues such as harassment and discrimination

2. First-hand information. Aside from data, directors benefit from exposure to employees from as many levels of the organization as possible. Paying attention to employee sentiment and behaviors can identify areas of strength or concern. This can be done by:

   - Getting a sense of the tone at the top through observation and the use of quantitative metrics
   - Observing interactions between management team members during board presentations to identify potentially unhealthy dynamics, such as top executives seeming wary of being candid
   - Interacting with employees below the C-suite during social events, site visits and board programs
   - Using the company’s products and services to interact with frontline employees and get a sense of its customer service style
   - Reviewing employee engagement surveys and requesting reports and presentations on corporate culture
3. **Accountability.** Focus from the board can ensure that developing and managing talent is one of a company’s top priorities. Directors should consider six actions as they broaden their roles to provide greater oversight:

- **Assign talent management responsibility to either the full board or a dedicated committee so everyone understands their roles and responsibilities.** Talent oversight is typically considered a full-board responsibility with committees overseeing the talent aspects associated with their areas of oversight. However, some boards assign responsibility to a designated committee. For example, 48% of compensation committees own human capital management oversight according to one survey.

- **Incorporate talent into strategy discussions.** When assessing the viability of strategic initiatives, directors sometimes focus on the financial implications of these decisions without discussing whether the company has the right people to execute them. One way directors can ensure that talent receives greater consideration in strategy discussions is to request that management include a “talent component” in every new initiative they present to the board.

- **Make talent management experience a key selection criteria for new board members and highlight existing capability.** Although not every board needs a director with human resources experience, broader talent management skills can be beneficial. Boards can prioritize recruiting directors who have managed entire divisions or regions to get those with greater talent management experience into their boardrooms. It’s also helpful to highlight this expertise among current directors in the company’s proxy statement. Keep in mind that leadership skills” of current and former CEOs can also be characterized as talent development experience, which would clarify for investors the extent to which the board has this expertise.

- **Elevate the chief human resources officer (CHRO) to a more strategic role and ask for regular updates.** Many companies have elevated their human capital leaders, giving them greater responsibility for overseeing talent development and culture efforts. As a member of the C-suite, the CHRO should have a regular spot on the board’s agenda. Some boards have their CHRO present a talent review to the entire board once a year, with updates as needed. This talent review should also include a focus on diversity and inclusion efforts.

- **Make talent management a KPI for executive compensation.** Establishing specific people-development metrics and goals in areas like diversity and inclusion, as well as retention targets for new hires and high-potential performers, can encourage leaders to place greater focus on talent issues. This requires having incentive plans with non-financial goals for the CEO and top executives rather than solely a focus on financial performance.

- **Ensure diversity and inclusion is embedded within the organization and that management provides appropriate reporting to the board on D&I goals and performance against those goals.** In addition, boards should continue to examine their own diversity and approach to succession planning, and should be transparent with stakeholders about their oversight efforts.
Building talent for tomorrow

The shortage of skilled labor, the astonishing pace of business and digital change, and demands from investors and other stakeholders are just a few reasons why boards need to shoulder greater oversight responsibility for talent management. While day-to-day development responsibilities should remain with management, directors need to ensure their company’s approach to talent supports the company’s long-term objectives.

When boards and management teams prioritize investing time and resources in human capital development throughout the organization, they are more likely to win the talent wars while becoming more agile, innovative and productive.

PwC perspective: communicating the board’s talent management approach in the proxy statement

Investors are increasingly interested in how boards approach oversight of talent. As part of providing greater transparency to investors, companies should consider the benefits of disclosing the following information in their annual proxy statements:

- How the board approaches its oversight of talent management
- How often the board discusses talent management issues
- How often these discussions include updates on the company’s diversity and inclusion efforts
- How executive leadership is held accountable for driving change in diversity and inclusion in the organization through metrics or goals-based compensation
- How the board plans for succession beyond the CEO
Appendix 1: Talent questions for directors to ask

### Overall strategy
- Do we have a workforce plan that forecasts our talent needs now and three to five years in the future?
- What’s our strategy for acquiring or developing that talent?
- What are the challenges to executing on our people strategy?
- Are we adequately investing in skill development, reskilling, upskilling, job redesign and alternate workforce models to address rapid technology advancements?
- Does senior leadership recognize the strategic importance of human capital?
- Does our CHRO have the right level of visibility in the boardroom?

### Diversity and inclusion
- How are we investing in recruiting, developing and promoting a diverse workforce? What are the results of those efforts?
- If we don’t have a diverse workforce, have we conducted a root-cause analysis to determine why, and decided how we will address the problem?
- Should we hold executives accountable through compensation metrics/goals?
- Should we consider adopting the Rooney Rule of interviewing at least one minority candidate for certain management positions?

### Succession planning
- How good are we at succession planning and following through on what we’ve decided?
- Are the executives two to three levels below the C-suite getting the experience and training they need to drive strategy—even completely new strategies?

### Board composition
- Does our board composition reflect the same diversity that we expect at the leadership level?
- Does the board have sufficient talent management experience? And to what extent have we prioritized this experience when recruiting new directors?
- In proxy disclosures, are we fully articulating the extent of talent management experience on the board?
- How should we assign responsibility for talent oversight on the board?
Endnotes


