The future role of the chair in Europe

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Chapter 11. The Future Role of the Chair in Europe

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This final chapter offers a forward-looking view that emerged from our research on how the chair's role and functions will evolve over the coming decade. As is often the case in the corporate governance domain, such changes will be evolutionary rather than revolutionary, but their impact will be felt across multiple dimensions.

In this chapter we identify changes pertaining to: i) the chair's demographic profile; ii) the role, tasks and capabilities of the high-performing chair in light of key developments; and iii) the impact of technology on the way in which the chair works.

This chapter focuses on an identifying and discussing three main drivers of the role and required capabilities of high-performing chairs over the next decade: a) shareholder activism and engagement, and sustainability; b) the increased frequency of business disruptions; and c) board leadership of corporate culture.

These factors will combine to make the chair's role not only more challenging and demanding, but also more important and indeed pivotal.[1] The chair will sit at the apex of the corporate governance system overseeing a more complex, more uncertain and ambiguous environment. As the next decade progresses, the chair's position will rise to prominence at the top of our organizations, eclipsing that of the CEO.

We begin by discussing some of the demographic trends we can currently observe regarding the chair position – and which we envisage continuing in the next decade. Next we discuss the three key factors that we believe will come to shape the chair's role and define the capabilities required to be effective in that position. A section then follows on how new technology in the boardroom will affect the chair's role. The chapter concludes by considering the balance of the chair's role in terms of monitoring versus stewardship.

Chair Attributes: Who will Occupy the Role over the Next Decade?

In ten years' time there will be more female chairs in European companies than there are today, yet they will remain in a minority everywhere. The legislative and regulatory pressures felt across Europe in recent years[2] – although perceived by many as insufficient – mean that more women will have the required board experience to become board chairs. A relatively recent study carried out by Credit Suisse Research Institute[3], on over 3,000 large companies globally, shows much progress in Europe compared to other world regions. The average female director representation in the sample was 24.4% in Europe, compared to just over 15% in the US. The trend differs from country to country in Europe, whether as a result of quotas or through voluntary compliance: as of now, even in countries such as the UK, where voluntary compliance is working relatively well, the number of women in chair

[1] Kakabadse, A., Kakabadse, N. and Barratt, R. (2006). Chairman and Chief Executive Officer (CEO): That Sacred and Secret Relationship. *Journal of Management Development*, 25(2), pp. 134-150

[2] International Finance Corporate (2015). A Guide to Corporate Governance Practices in the European Union. Available from: https://www.ifc.org/wps/wcm/connect/c44d6d0047b7597bb7d9f7299ede9589/CG_Practices_in_EU_Guide.pdf?MOD=AJPERES [Accessed 3 December 2018]; Jourova, V. (2016). Gender Balance on Corporate boards: Europe is Cracking the Glass Ceiling. European Commission Fact Sheet. Available from: http://ec.europa.eu/newsroom/document.cfm?doc_id=46280 [Accessed 3 December 2018]

[3] Dawson, J., Kersley, R. and Natella, S. (2016). The CS Gender 3000: The Reward for Change. *Credit Suisse Research Institute.* Available from: http://publications.credit-suisse.com/tasks/render/file/index.cfm?fileid=5A7755E1-EFDD-1973-A0B5C54AFF3FB0AE [Accessed 3 December 2018]

positions in the FTSE 100 is very low, although there has been good progress at the non-executive level, with 35.3% of these roles held by women.[4] In addition, 24% of board committees in the FTSE 100 are now chaired by a female director.[5] Such progress will translate into some of these directors attaining the board chair position in the next decade, not just in the UK but in other European countries as well.

As far as age is concerned, chairs will continue to be older than executives, with many professionals in their seventies and even eighties continuing to lead boards. The increase in time and effort demanded by the role – as well as the new capabilities that complexity and technology will necessitate – may mean that there will be more chairs in their forties and fifties.

Board leaders' backgrounds will be more diverse than they are today, but the CEO/general management route will remain the main career path for the job.

"Celebrity chairs" – those chairing boards on account of their personal prestige alone – will almost disappear. Prestige will secure a chair position only if accompanied by capability and a clear contribution to governance and performance.

Overall, the profile of the chair will change slowly over the next decade to include more women, younger people and fewer celebrities. In addition, although CEO/general management will remain the main avenue, a wider range of backgrounds will be considered, with the role increasingly addressing topics such as stakeholder engagement, sustainability and corporate culture.

Chair work: Three Key Factors Shaping the Role

A number of factors will influence the nature of the role and the capabilities required to be a high-performing chair. These factors also mean that chairing a board will require a greater time commitment, with fewer chairs therefore occupying more than one such position. Chairs will be busier and their focus will be split between running the board (including their relationship with the CEO) and engaging with shareholders and a variety of other stakeholders. Chairs will find themselves more frequently called upon to lead through a particular crisis or disruption. They will need to pay more attention to their task of overseeing corporate culture and creating the right conditions for the board to function as an effective steward of the appropriate culture for the business. These factors are discussed in greater detail in the following sections.

Shareholder Activism, Engagement and Sustainability

The push by European authorities for increased shareholder rights and a stronger shareholder voice in the affairs of corporations – as exemplified by the Shareholder Rights Directive (SRD)[6] and the UK Stewardship Code[7] (due to be revised) – means that chairs will have to pay greater attention to the voices of shareholders and act as effective bridges between shareholders, the board and management. Emerging policy and regulation is advocating improvements in dialogue between companies and investors, e.g. through the creation of stakeholder advisory panels and annual reporting on how companies engage with stakeholders.

The potential for improving the effectiveness of corporate governance is high, but it could also be a recipe for tensions at the top if not handled carefully. PwC's annual corporate director survey indicates that, while shareholder engagement has become more common in recent years (54% of the 884 directors of public companies surveyed state that their board is involved in direct engagement

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[4] Vinnicombe, S., Doldor, E., and Sealy, R. (2018). The Female FTSE Board Report 2018: Busy Going Nowhere with the Female Executive Pipeline. Cranfield University. Available from: https://30percentclub.org/assets/uploads/UK/Third_Party_Reports/2018_-_CranfieldFemale_FTSE_Board_Report.pdf [Accessed 3 December 2018]

[5] Ibid.

[6] European Parliament (2017). Directive (EU) 2017/828 of the European Parliament and the Council of 17 May 2017. *Official Journal of the European Union*, L 132. Available from: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017L0828&from=EN [Accessed 3 December 2018]

[7] Financial Reporting Council (2012). The UK Stewardship Code. Available from: https://www.frc.org.uk/getattachment/d67933f9-ca38-4233-b603-3d24b2f62c5f/UK-Stewardship-Code-(September-2012).pdf [Accessed 3 December 2018]

with investors), not all corporate directors view this as beneficial, with 21% reporting that they derived no valuable insights from such engagement.[8] Chairs will therefore become the focal point of governance, and their ability to reconcile competing agendas and build trust is going to be stress-tested to the maximum. They will have to create meaningful and proactive engagement with investors, and manage the frustrations that this process may bring for the various parties. However, a more recent report[9] suggests that, in considering a range of chair tasks, only 36% of respondents consider chairs to be very effective at communicating with shareholders (46% view them as somewhat effective and 24% as ineffective), with this competence scoring lowest of all categories of chair task effectiveness.

Chairs will have to engage with shareholders over a great range of topics beyond financial performance and executive remuneration. The pressure for firms to strategically integrate, monitor and disclose material environmental, societal and governance (ESG) issues is increasing[10] but is yet to be taken seriously, even by those boards whose firms report on sustainability.[11] This will change. The head of engagement for a large institutional investor recently told us:

> *Concerns over climate change and how these concerns are being integrated in investees' strategies is growing in the investment community; there is also a renewed push for better assessing social impact, one of the aspects of ESG that often got forgotten. I think this will become very relevant over the coming years – as firms and investors learn how to effectively engage and mind-set change starts to build.*

For many chairs, this will represent a shift in mind-set and practice. Their thinking will need to become more holistic, boardroom debate will need to move from traditional ways of looking at value creation to include social and environmental considerations; perhaps a non-executive director will need to have specific responsibilities for sustainability; an executive committee may need to report directly to the board; and CEO performance and incentives will need to be designed to reflect investors' ESG concerns. Sustainability performance is not just another fashion concept that will fade with time. It is here to stay and will be a tremendous source of competitive advantage in the not-too-distant future.

Greater shareholder involvement also means that chairs will be under closer scrutiny, and face removal if they fail to take due and balanced consideration of shareholder concerns. There is the possibility that the length of chair tenure will be reduced over the coming decade: as the role grows in importance and influence, and is subject to greater scrutiny, only the most outstanding chairs will have a secure place.

More Frequent and More Complex Business Disruptions

Business disruptions are becoming more frequent and more complex. Since the turn of the millennium we have witnessed: technological innovations disrupting entire industries (e.g. music, transportation);

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[8] PricewaterhouseCoopers (2016). The Swinging Pendulum: Board Governance in the Age of Shareholder Empowerment. PwC's 2016 Annual Corporate Directors Survey. Available from: https://www.pwc.es/es/publicaciones/consejos-y-buen-gobierno/2016-annual-corporate-directors-survey.pdf [Accessed 3 December 2018]

[9] PricewaterhouseCoopers (2018). The Evolving Boardroom: Signs of Change. PwC's 2018 Annual Corporate Directors Survey. Available from: https://www.pwc.com/us/en/governance-insights-center/annual-corporate-directors-survey/assets/pwc-annual-corporate-directors-survey-2018.pdf [Accessed 3 December 2018]

[10] KPMG (2017). ESG, Strategy and the Long View: A Framework for Board Oversight. Available from: https://assets.kpmg.com/content/dam/kpmg/lu/pdf/lu-en-esg-strategy-framework-for-board-oversight.pdf [Accessed 3 December 2018]

[11] Kiron, D., Kruschwitz, N., Haanaes, K., Reeves, M., Fuisz-Kehrbach, S. and Kell, G. (2015). Joining Forces: Collaboration and Leadership for Sustaninability. *MIT Sloan Management Review*. Available from: https://sloanreview.mit.edu/projects/joining-forces/ [Accessed 3 December 2018]; UNEP (United Nations Environment Programme) (2014). Integrated Governance: A New Model of Governance for Sustainability. Available from: http://www.unepfi.org/fileadmin/documents/UNEPFI_IntegratedGovernance.pdf [Accessed 3 December 2018]

more frequent reputational crises fuelled by social media; systemic and global financial meltdowns; prolonged recessions; and continuous political instability. The world has become a riskier place according to 56% of respondents to the World Economic Forum Global Risks Report 2018.[12] The report highlights key fundamental concerns: the increased risks of extreme-weather events; political and economic confrontations between major powers; cyber-attacks; and the persistent underlying weaknesses of global financial systems.[13] At the corporate level, CEOs appear more optimistic with 57% believing that global growth will improve (but only 45% for the European Economic Area, seemingly the least optimistic of all world regions). In Europe, CEOs identify lack of availability of key skills (51%), over-regulation (48%) and political uncertainty (42%) as the top three threats to their organizations' growth prospects.[14]

Navigating these increasingly turbulent waters, developing crisis management skills and bringing together different parties to reach shared solutions are tasks that are increasingly likely to fall to the chair. The uncertain business landscape will see corporations more frequently shifting consensus at the top on how they should be governed and directed, and strategic tensions will likely be exacerbated.[15] Chairs have long been depicted as playing a greater role during upheaval and disruption.[16] A recent large US study showed that, in contexts of high complexity and resource scarcity, chairs account for up to 9% of variation in firm performance over and above the variation explained by the CEO.[17] The coming decade will see more chairs called upon to step up and lead directly from the board in times of upheaval – as these disruptions will require more collaborative leadership, as opposed to an archetypal strong, dominant CEO saving the day. Chairs will be required to equip their boards with the capabilities they need to face up to different types of threats, both by ensuring a diverse board composition with the right mix of skills and experiences, and also by developing scanning and sense-making processes to enable effective directional responses to emerging issues. Chairs will also need to ensure that their board comprises individuals who know how to operate in a time of crisis or disruption – skills that have often been acquired in addressing extreme circumstances elsewhere. Finally, chairs will need to ensure that their board can raise uncomfortable issues and vigorously debate them on a regular basis: setting the tone for robust debate about tension-generating topics while ensuring board cohesiveness will be all the more challenging in the years to come. Chairs that combine this capability with an evidence-based approach, along with proficiency in stakeholder engagement and a long-term focus, will be better equipped to succeed in turbulent times.

Shaping Corporate Culture

Peter Drucker has been credited with the quote "culture eats strategy for breakfast", an idea which has become the subject of much debate. It is an assertion that is increasingly recognized by regulators[18], with organizational culture cited as the basis of the 2008 financial meltdown along with

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12 World Economic Forum (2018). The Global Risks Report 2018: 13th Edition. Available from: http://www3.weforum.org/docs/WEF_GRR18_Report.pdf [Accessed 3 December 2018]

13 Ibid.

14 PricewaterhouseCoopers (2018). 21st CEO Survey: The Anxious Optimist in the Corner Office. Available from: https://www.pwc.com/gx/en/ceo-survey/2018/pwc-ceo-survey-report-2018.pdf [Accessed 3 December 2018]

15 Morais, F., Kakabadse, A. and Kakabadse, N. (2018). The Chairperson and CEO Roles Interaction and Responses to Strategic Tensions. *Corporate Governance: The International Journal of Business in Society*, 18(1), pp. 143-164

16 Mizruchi, M.S. (1983). Who Controls Whom? An Examination of the Relation between Management and Boards of Directors in Large American Corporations. *The Academy of Management Review*, 8(3), pp. 426-435; Parker, H. (1990). The Company Chairman: His Roles and Responsibilities. *Long Range Planning*, 23(4), pp. 35-43

17 Withers, M.C. and Fitza, M.A. (2017). Do Board Chairs Matter? The Influence of Board Chairs on Firm Performance. *Strategic Management Journal*, 38(6), pp. 1,343-1,355

18 Financial Reporting Council (2018). The UK Corporate Governance Code. Available from: https://www.frc.org.uk/getattachment/88bd8c45-50ea-4841-95b0-d2f4f48069a2/2018-UK-Corporate-Governance-Code-FINAL.PDF [Accessed 3 December 2018]

other corporate failures. An early report by the Financial Reporting Council[19] showed that boards acknowledge the responsibility of determining the purpose of the company (why it exists, beyond merely generating profit), and therefore the values and behaviours that are required to fulfil its purpose. Yet "culture" is perceived by many chairs as simply the determination of strategy: the rate of expansion, the markets in which the company is likely to succeed, the mode of entry, and so on.[20]

Although regulators are paving the way for culture to feature high on board agendas, boards are yet to attach any importance to this critical governance function. Nor have they developed any means by which to fulfil their responsibility to assure shareholders and other stakeholders that the culture of the firm is healthy and conducive to sustainable business performance.

Recent research by Board Agenda and Mazars, in association with INSEAD, has revealed that much work awaits chairs in ensuring that their boards can be effective stewards of the corporate culture.[21] Boards either fail to value culture as a topic or are simply ill equipped to handle it, yet many recognize the existence of fractures between strategy and culture. Directors generally assume the principal ways to influence corporate culture are to set the right tone from the top, ensuring the CEO is supportive of the desired culture, and making the right appointments to the board and senior management. A recent survey shows that, currently, in assessing culture, approximately 66% of directors rely on gut feeling based on interactions with management, yet only 32% believe this is effective.[22] However, our own research suggests that non-executive directors' (NEDs') informal contact with a company's operations and people is an invaluable resource complementing more formal ways of assessing corporate culture. With many CEOs still feeling nervous about allowing NEDs to visit operations and talk with other layers of management, chairs need to ensure that these activities happen, so as to enable NEDs to have a line of sight into the corporation's culture. It is up to the chair to set the tone for culture – and that starts in the boardroom. One chair recently told us:

> *A wildly underplayed aspect of board performance is culture, values and behaviours. So for me the big difference is, and we know this from sitting on boards: you can have exactly the same people sitting around the board table, but with a different style of chair you will get a completely different dialogue but with the same people.*

Many leading firms with enlightened boards and chairs are actively promoting breakfasts in which NEDs meet employees from different parts of the organization, inviting employees to present to the board and enabling NED visits to operations. These companies' CEOs do not regard such practices as stepping into their territory but rather as ways in which NEDs can be more useful and bring more value to the table. One highly experienced FTSE 100 chair commented on his approach:

> *Non-executives can go into executive meetings, R&D, product marketing, visit any research establishment, any manufacturing or commercial unit, find out what's going on… no chaperoning, and initially I said, go and be a fly on the wall but if you need to ask a question, ask a question, and that is now part of the way the company operates. And I always had that right, if you like, but I wanted to make sure all my board members did.*

In the future high-performing chairs will routinely start every board meeting by reminding board members of the purpose, values and behaviours that are integral to the firm's culture. They will be

[19] Financial Reporting Council (2016). Corporate Culture and the role of Boards: Report of Observations. Available from: https://www.frc.org.uk/getattachment/3851b9c5-92d3-4695-aeb2-87c9052dc8c1/Corporate-Culture-and-the-Role-of-Boards-Report-of-Observations.pdf [Accessed 3 December 2018]

[20] Ibid.

[21] Board Agenda and Mazars (2017). Board Leadership in Corporate Culture: European Report 2017. Available from: https://www.mazars.com/content/download/914232/47476119/version//file/Board%20Leadership%20in%20Corporate%20Culture%20Report.pdf [Accessed 3 December 2018]

[22] PricewaterhouseCoopers (2018). The Evolving Boardroom: Signs of Change. PwC's 2018 Annual Corporate Directors Survey. Available from: https://www.pwc.com/us/en/governance-insights-center/annual-corporate-directors-survey/assets/pwc-annual-corporate-directors-survey-2018.pdf [Accessed 3 December 2018]

crystal clear in identifying the types of behaviours that are not tolerated, and swift and assertive at addressing them if they do occur.

Technology Adoption By Boards: How will It Change the Way the Chair Works?

The impact on technology on boards – and therefore on the work of the chair – is growing. A recent report by consulting firm Forrester (2018) indicates an increasing, albeit slow, take-up of technology by boards in Europe, but also highlights growing concerns. About 45 percent of boards in Europe already have board-management software with one-to-one/group chat capability. Many also have minute-taking, archiving and search capabilities, voting/pooling, virtual deal rooms (VDR) and much more.[23] This enables board members to be more effective, as they can quickly access information, scorecards and reports in a way not possible a few years ago, allowing them to attain fresh insights and ask better questions. This is all the more important when we consider that reporting requirements are on the increase, the tracking of ESG performance being one example. However, 42 percent of European directors have concerns about breaches of data, fearing the exposure of sensitive information on a large scale; and over 50 percent of boards that use board-management software reported it as being unhelpful during a crisis in terms of responding within time constraints and assuring good communication between directors.[24]

The way board members interact will continue to change in the coming decade, and this may have profound implications. If every board activity is recorded and undertaken remotely (i.e. online), a possible outcome is that directors may be (even) less inclined to have those difficult conversations for fear of them being recorded and subsequently either leaked to the press or used against them in a lawsuit by an aggrieved shareholder or other stakeholder. Also, online communication has a greater potential for misunderstandings, in comparison with face-to-face, as behavioural language is important in conveying meaning. On the positive side, online communication may make less talkative board members feel more willing to contribute – even if handling disagreement proves more difficult. Chairs will need to be on top of this and use technology in a way that maximizes efficiency of board operations without jeopardizing relationships and quality of debate.

Conclusion

In the coming decade, chairs in Europe will be required to collaborate more extensively, both internally and externally, in order to seek shared solutions to frequent and complex business disruptions.

Their focus will be divided between, on the one hand, the more traditional roles of oversight and relationship with the CEO and, on the other, a greater emphasis on stewardship in terms of shareholder engagement, sustainable performance and corporate culture. The chair will become the guardian of the long-term view of the firm and the one individual who reminds everyone – board members, executives and shareholders – of the higher purpose that the firm serves, maintaining quality of engagement and ensuring the alignment of the different and shifting interests in and around the boardroom.

Such a shift in emphasis will require chairs to become more available, which will often include leading the company through difficult situations. The skill-set of the high-performing chair must

[23] Forrester Consulting (2018). Directors' Digital Divide: Boardroom Practices Aren't Keeping Pace with Technology. Too Many Boards Still Use Personal Email and Fail to Adopt Technology for Sensitive Communication. Available from: https://diligent.com/wp-content/uploads/2018/10/Global-Report-Forrester-Directors-Digital-Divide-Boardroom-Practices.pdf [Accessed 3 December 2018]
[24] Ibid.

expand to include holistic thinking, political savviness, long-term vision, and an ability to reconcile competing agendas and gather the support of external stakeholders.

One effect of the chair's changing role is that the profile of the senior independent director (SID) will also need to rise. SIDs will need to understand how the chair's role and prominence is expanding, and develop their skills in new domains in order to be in a position to support and/or challenge the chair when required.

The conclusions detailed above point to our most significant prediction all. That is, the role of chair is set to become the most important in contemporary organizations, surpassing that of the CEO. Welcome to the age of the board chair.

Resources for the Chapter 11:

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