

The Board and HR

By David Creelman and Andrew Lambert



How do boards oversee human capital? That was the question we set out to answer in our study “HR and the Board: How board oversight of human capital works” that was released in 2011

We conducted a study in which we interviewed CHROs and HR directors — together with a number of other board directors, including a CEO and chairman — from 28 organizations handpicked for their good reputation, mainly large and global, headquartered in the United States and the United Kingdom and from a wide range of sectors. We focused on what the best companies are doing, not the average ones, as we were most interested in how to do it right, not bemoaning the lack of progress in many companies.

The results were hopeful, but also challenging. Good boards really do spend a lot of time reviewing culture, leadership and other elements of human capital. But this puts new demands on the CHRO to be “board capable.” We also found that, in many cases, the HR leader is getting pulled into an important role in the internal workings of the board and interacting with many committees. Some CHROs are fully ready for this bigger role; others will find it puts them at risk.

We have heard some not-so-good boards say, “Oh yes, our board spends a lot of time on human capital, too,” but mean only that they devote a good deal of time to executive reward and CEO succession. Frankly, while important, these topics were of minor interest to us for this particular study. Copious work is being done on executive reward and CEO succession. We were interested in what went on beyond those old, if still debate-raising, areas. In this paper, we will share our findings on the new, more extensive work boards are doing in overseeing human capital and how that affects their interaction with HR.

Understanding the Issues

There are two separate issues around the board’s relationship with HR. The first is that human capital — however you want to define it — is an increasingly important driver of value creation. The idea that a board can successfully protect shareholders interests without having a good handle on issues like talent and culture is archaic.

The second issue is the growing recognition that corporate governance has often been inadequate. There are many, possibly too many, ideas about how to improve governance, but it is inescapable that many governance problems relate to how board members are selected, developed and evaluated — all classic areas of HR expertise. In addition, increasingly boards find they need the top “people person” — if they are up to it — to play the role of interlocutor between nonexecutive and executive directors, helping to manage relationships between the key players.

Both issues put new pressure on the HR leader to be “board capable,” something we will discuss at greater length later in this article. It also puts pressure on the board to be “human capital savvy,” and it is often hard to find people who have a deep knowledge of talent and culture and who also have the requisite general management experience to serve on a board.

How Do Boards Keep an Eye on Human Capital?

Assume for the moment that the board complies with official governance requirements and that it is functioning smoothly. Nonetheless, how do they know that the organization is not, to put it bluntly, screwing up on human capital?

Here is how Randy MacDonald, senior vice president of human resources for IBM, frames it:

As a shareholder, I want to know the organization has the very best people they can possibly have deployed, and I want to know that the leadership has the strategic view and operational drive to make that happen. Too many corporations over the years have focused too narrowly on the numbers, only to find the skill sets they needed to drive performance just weren’t there.

For effective oversight of human capital, boards should apply both supply and demand perspectives.

- A capabilities lens (supply) examines the broad question “Is our human capital strong?” and concerns issues such as depth and breadth of skills and talent, succession, engagement and diversity.
- A people lens (demand) looks at business questions, such as growth, innovation, risk, M&As, restructuring, and new products and systems and then asks what the people implications are.

The Capabilities Lens

Traditionally, boards concentrated on the selection, performance and reward of the top executives and their potential successors. In the last 10 years, boards have devoted increasing attention to a wider talent pool. The CHROs we spoke to would often talk in terms of the “top 100” (or more) to indicate the talent pool that not only played an impor-

Top ‘Must Dos’

- **Take the lead:** Don’t wait for the board to ask for human capital insights. Inject thoughtful review of people issues into discussion of strategy and reputation before trouble occurs.
- **Have a plan:** It takes time to educate board members, but board time is short. Plan how to use limited opportunities to have a cumulative effect over time.
- **Use a framework:** There are many categories of people issues — from managing the board itself to HR risk to engagement — so use a framework to stay on track.
- **Build relationships:** Get to know the board members — their strengths, interests and quirks. Become the trusted guide for both the CEO and the board.
- **Get HR-savvy board members:** Boards often have no one with a deep understanding of talent and culture, so help the nominations committee find people who are HR-savvy.

The board needs sources of information about HR.

tant role in the success of the company today, but were also the prime candidates for filling the C-suite in the future. Boards want to know who these people are, who is new, who has left and how they are doing.

Beyond a focus on leadership, we found that boards exercising full responsibility for human capital have an interest in the way the entire workforce is managed. Stephen Dando, executive vice president and chief human resources officer for Thomson Reuters, told us: “Employee engagement is certainly something any board should be interested in. It’s not a ‘nice to have,’ but fuel in the tank for superior business performance.”

The important broader workforce issues vary from company to company but can include things such as culture, skills, diversity, industrial relations, health and safety, customer focus and employment brand.

The People Lens

The people lens discussion depends entirely on the nature of the business issues and the sophistication of the board about HR matters. While set yearly or twice-yearly examinations of people strategy are the norm, a people-focused board considers the human dimension in every business discussion.

When the people lens is applied to business issues, it often becomes a discussion about leadership. The board wants to be assured that the company has sufficient leadership talent behind any important initiative and that it will not go awry.

They may also consider broader talent issues, such as one case where the rollout of a new product was dependent on hiring a large number of technicians — delays in hiring those relatively low-level employees could derail the strategy. In another case, the issue was a mismatch between the self-image of a global company and the small number of people who had global experience; the board recognized that the lack of worldly leaders would inhibit their ability to compete internationally. And there will be cases where boards have failed to apply the people lens, for example, not recognizing how management was driving the union toward a damaging strike.

A Significant Investment of Time

In aggregate, discussion on people issues can take 25-35 percent of a board’s time. Yet the hours invested can still seem small given the task at hand — spending a couple of hours reviewing the top 100 people does not lend itself to an in-depth discussion of potential.

The board’s constrained time frame reminds us that the board is providing oversight on human capital, not managing it. It might be better to see a “top 100 review” not as the board actually keeping an eye on individuals, but looking for indications that the talent management processes are effective and that executive teams’ more lengthy reviews of talent are done well. But being good at this is not just about time. Instead, improved effectiveness will derive from better quality of discussion and becoming skillful at identifying which people issues have the greatest impact on performance and future business prospects.

Sources of Information on HR

To apply either the people or capability lenses, the board needs sources of information about HR.

The first thing that comes to mind is the written material in the “board pack.” Yet, interestingly, we found that none of the directors or CHROs talked excitedly about the great board packs they used and the difference it made. It would be wrong to jump to concluding that board packs don’t matter — of course they do. In fact, there was some good advice about keeping them short, reporting on factors like “comings and goings” in the senior ranks, reporting on engagement scores, people risks and so on. One CHRO emphasized the value of consistency in board pack formats so that board members become familiar with it; others talked about the need for variety. But board packs clearly play a supporting role to high-quality discussion, and, thus, better board packs are not the main route to better oversight of human capital.

Furthermore, despite the continuing debate within HR about HR metrics, our interviewees were most inclined to emphasize the important of qualitative factors. Eva Sage-Gavin, EVP of global human resources and corporate affairs for The Gap, said:

What is critical is the qualitative element and how it drives and supports our business strategy. This is why we always do a three year look-back of where we have been and what we have learned, then conduct a three year look-forward and determine the implications for our business and how well-prepared we are to address them.

There is an important lesson here for those within the world of HR who are fond of the idea of a human capital balance sheet that mimics financial reporting. While there are certainly advances to be made in measuring human capital, none of the CHROs we interviewed saw this as a key factor.

Boards found two particular sources of information to be helpful. The first was presentations that stimulate. This is best understood by imagining the opposite: a tedious presentation of slides about the employee survey or a recitation of a long list of HR programs. Presentations that stimulate are characterized by focusing on insights, not data, which requires that HR is business-savvy.

Second, there was the central importance of discussion. Whenever CHROs talked about effective boards, they ended up telling us about the debates that took place. Again, this is easiest to envisage by imagining the opposite: a board sitting politely and nodding as HR walked through their material. The value of open board debate is that it challenges management, provides fresh insights for the organization and helps the board itself develop a clearer understanding of the issues.

Another important finding was how much boards valued the information they got about HR outside of the boardroom. The most common way this happened was around dinners after board meetings where board members could socialize with senior leaders and high potentials. However, several interviewees stressed that this was insufficient; board members should spend time on unescorted visits to the organization. Only by getting out of the top floors of headquarters and into the guts of the business could they get a feel for whether the information they were getting was accurate or not.

As one nonexecutive director told us: “You need to look at the metrics as a piece of ‘hygiene,’ but you have to be a little skeptical. It’s essential to understand the context, or you can delude yourself that everything’s fine.” That context comes from getting outside the boardroom.

Who Is the Driver of Good Oversight?

It was rare to hear about boards telling HR what kind of information they needed about human capital. It is almost always the CHRO who has taken the lead in gathering the information, defining the issues and educating the board. These were handpicked organizations, and we would hear repeatedly that the board was supportive. We did not uncover cases where a CHRO had gone up against an unsympathetic board and managed to change the agenda (which is not to say it’s impossible, but that was not the happening within the group of organizations we studied). Clearly, organizations need a CHRO who will take the lead in driving the agenda. Truly unsympathetic boards who think people issues don’t matter are rare, and so if HR makes the effort to present compelling, discussable content, then, over time, the board can be developed to provide good oversight of human capital.

HR’s Role in Board Matters

Not surprisingly, in companies where the board is paying attention to human capital, HR has taken on a bigger role in board matters. Michael Robinson, global head of human resources for MAN Group, told us that “Over the past six to seven years, my attendance at board meetings has increased exponentially — and it’s by no means all about remuneration.”

HR leaders’ role is increasing in three areas. First, they are involved with more committees — and often all of them — not just the compensation committee. Next, increasingly they play a role in boards’ own people processes: assessment, selection, development, performance review, etc. Finally, as the “people person,” they may find themselves “holding up the mirror” to the board in terms of values, as well as acting as an interlocutor between key players, for example between CEO and chairman where these roles are separated.

Let’s look at each of these three areas.

Board Committees

Nonexecutive directorships in developed markets like the United States and the United Kingdom are generally no longer cushy jobs for members of the old-boys network, but roles imbued with heavy responsibilities. One way of handling the increasing responsibilities is to use committees to increase focus. Audit committees and now compensation committees are increasingly in the public spotlight.

Different companies do things different ways. In Diageo, all board members are on all committees. That’s unusual, but it works for them. The consensus was that there was no need to converge on a single model for design of committees, but simply to find an arrangement that fit the organization. For HR, the most important change is that people issues are increasingly recognized as relevant to the agenda of all committees, not just compensation.

The audit committee is concerned with the quality of information provided to shareholders, including the quality of human capital insights and what this says about an organization’s long-term future. Also, it is here that responsibilities lie for handling whistleblowing; they may look to the CHRO to discuss the culture and procedures about that.

While people risks of various kinds straddle most committees’ agendas, any risk committee should discuss HR risks with the CHRO. This interest in people may be quite new. One CHRO said, “Our risk committee covers people risks now —but it didn’t two years ago.”

Clearly, the compensation committee demands a lot from the CHRO, and governance pressures are encouraging greater rigor in ensuring that reward is healthily performance-related and not driving risky behavior — particularly in financial services. Another committee that should interact with the CHRO is the nominations committee, partly to ensure that selection processes for directors are robust. We found that both needed to understand talent issues in order to perform effectively.

Committee workloads are increasing, and so is the use of advisers, for example, on pensions, remuneration, recruitment and other people issues, separately from those a company may use already. Nonetheless, both in selecting and getting the best out of advisers, boards have good reason to consult the person who should be expert on the HR supplier market.

Should there be an HR committee? Increasingly, compensation committees are broadening their remit and renaming themselves. However, all board directors should understand all risks. One CHRO was adamant that HR committees were a bad idea. “We don’t need an HR com-

Further reading:

The Human Equation: Building Profits by Putting People First, Jeffrey Pfeffer (1998), Harvard Business School Press

The Effective Board, Neville Dr Bain & Roger Barker (2010), Kogan Page

Seven Questions Boards Should Ask Chief HR Officers Joseph E. McCann III, (March 2006) Directors Monthly

Human capital management: what are boards doing? Ed Lawler (2009) Marshall School of Business Working Paper No. MOR 21-09, research@marshall.usc.edu

Board Dynamics - The Chairman’s perspective, IDDAS (2010) www.iddas.com

Organizations in Depth: The Psychoanalysis of Organizations, Yiannis Gabriel (1999), Sage Publications

The behavioural drivers of board effectiveness, MWM Consulting (2010) www.mwmconsulting.com

Why the Bottom Line ISN’T! How to Build Value Through People and Organization, Dave Ulrich and Norm Smallwood (2003), Wiley

Reporting on Human Capital: What the Fortune 100 Tell Wall Street about Human Capital 2nd Edition, Creelman Research and RBL Group (2010)

The Chief HR Officer: Defining the New Role of Human Resource Leaders, ed. Patrick Wright (2011), Wiley

Configuring HR for Tomorrow’s Challenges, Andrew Lambert (2009), Corporate Research Forum – see especially chapters on HR & governance; role of HR director www.crforum.co.uk

Managing the People Dimension of Risk, Andrew Lambert & David Cooper (2010) Corporate Research Forum www.crforum.co.uk

Talent: Making People Your Competitive Advantage Ed Lawler (2008), Jossey-Bass

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mittee,” he said. “‘People’ is a matter for the entire board, in our view.”

However, our own conclusion is that there are many different ways of organizing board committees. While it is important that there is oversight of the various people issues, it matters less where in the board they are covered.

The Board’s Own People Processes

HR has a role to play in improving the board’s own people processes. Historically, board members were considered to be so seasoned that development was unnecessary. Now, the focus on governance has opened the door for a review of the board’s own people processes, including recruitment, development and appraisal — all core areas of HR expertise.

The headline issue in recruiting board members is diversity, but this should be seen in light of the broader issue of whether the board has the range of talent it needs, not only whether it has the right mix of gender and ethnicities.

In the interests of oversight of human capital, should boards recruit members with some kind of HR background? Very few do. Why?

The most favored recruits are finance experts and CEOs, and then well-connected people in fields useful to the particular business sector, such as scientists. The assumption is that “general managers” have to know enough about people to have got to the top. There was relatively little interest in recruiting HR specialists because they were perceived to have too little business knowledge, rightly or wrongly.

Yet we also found many flaws in this situation. CEOs were generally not observed to know what good HR looked like — with a few honorable exceptions — and a board made up of strong, controlling personalities is liable to be dysfunctional. Second, we heard that a preponderance of financial specialists tended to feature major blind spots due to narrowness of perspective. Third, many company chairmen needed help with managing “team issues” and relationships with CEOs — and, incidentally, they themselves observed that many CEOs are behaviorally ill-equipped to be chairmen. And, lastly, we found that boards generally didn’t have enough skills in areas such as organization design and development, managing change and psychology — all skills that are necessary for good oversight of the

people aspects of business strategy, performance and top team behavior.

Developing board directors is one of those things that seems like a good idea, but due to constraints on time, it can be easier to get attention for briefings on technical subjects than to address soft issues such as teamwork. That said, some nonexecutive directors told us that they now discuss how the board works together far more than in the past.

We also had CHROs who clearly had an agenda of educating the board about HR issues over time. It was not called a development program; it was just a by-product of how they presented information. But it was clear in many cases that HR had a long range objective to enhance the board’s ability to understand people issues.

There is now more pressure on boards to have their performance reviewed both internally and periodically by external experts. This tends initially to be driven by the chairman with the company secretary. However, we did find recourse being made to respected HR leaders to play a key role.

One CHRO noted: “External board assessors are a variable bunch. We’ve done one, but I’ll certainly be recommending something more robust to my chairman for next time.” Another said: “We have applied a lot of science to our board evaluation. And they said it was the best feedback they ever had.” Clearly, a CHRO should be able to offer sound advice on getting effective feedback to the board, as well as on review methodology and use of suppliers in this sensitive area.

Being the ‘People Person’

In our informal discussions with CHROs, they were more inclined to talk about personalities and politics than the more technical side of “good human capital oversight.” This is not just idle chatter, one CHRO commented: “The importance of relationships at the top can often be underestimated. Where that applies, you see the lack of investment of time and energy — and then there’s a price to pay.”

There is often an expectation that the HR leader will play a special role in facilitating teamwork and even act as a critical neutral party in managing the relationship between the chairman and CEO where those roles are separated. It also often falls on the HR leader to be the guardian of values and hold up the mirror

to board members and senior leaders when they are not living up to the company’s espoused values. “This should not be about being ‘holier than thou’ — it’s good business to do conduct your business well,” commented one CHRO.

Board-Capable HR

This study has left us with our own impression of what makes an HR leader capable of working effectively with the board. It is useful to make the distinction between what we should expect of any functional head (but has not always been demanded of HR) and what additional attributes are required in a board-capable CHRO.

The standard functional head requirements are being a business person first and foremost, being the expert in your domain and being able to deliver results. HR leaders are typically respected for their skills in the latter two of these criteria, but the function is still too often perceived to be insufficiently business-savvy.

The additional attributes include the relationship skills to manage the strong personalities at the top of the organization, having expertise in governance, understanding HR risk, being able to win arguments when necessary, and having the gravitas to act as a strong proponent of corporate values.

Jill Smart, chief human resources officer at Accenture, said: “It’s more than having us report data to the board. We have rich and productive discussions with our board, and this exchange of perspectives with the board members contributes to new thinking about the future.”

Do you really need board-capable HR? One of the nonexecutive directors we interviewed was clear that it did matter. “If the HR head isn’t of the right caliber — and it can certainly be patchy — there’s a void,” he said. “It affects lots of things, starting with the quality of appointments. A chief executive doesn’t necessarily know what a good HR director looks like, and boards themselves may not understand the key executive roles. That’s why we need experienced nonexecs.”

Conclusions and Challenges

We found there is no longer any question as to whether good boards take HR factors seriously. People issues are a major concern for any “good” board, for example, the perfor-

mance and development of the board itself, the top team, the succession and talent pool and the broader workforce.

Increasingly, the CHROs we interviewed felt that applying a people lens to business issues was not just being done better, but that it was becoming second nature.

In companies where HR sits on the sidelines, for the sake of good governance, these companies should change this model. “Our board is fully engaged in reviewing any large scale organizational development or change initiative, from concept to tracking progress. Obviously that covers acquisitions. Also, anything important that might get in the press. And we certainly don’t wait until board meetings to keep them up-to-date,” said Gareth Williams, human resources director at Diageo.

Does it make any difference that boards are paying attention? There were a few skeptics who thought that it was only the executive committee that mattered, not the board itself. However, the majority opinion was that the board did have an impact by asking pointed questions, drawing on their own experiences, providing a stamp of authority to HR decisions and policies, and creating accountability for better people management. As soon as managers know the board will be looking at an issue, whether that is employment brand or succession or HR risk, then it directs management attention there, and that is often where the impact lies.

When boards decide to take HR more seriously, it truly changes the job of the CHRO. We found the role of high-achieving CHROs has shifted toward adding value to the board as well as to the executive team. Top CHROs are increasingly called upon to facilitate relationships not only between the CEO and top team members — including their performance and development — but also where necessary between chairman and CEO. At times of tension, the role becomes one of interlocutor and can also involve the senior independent director (or equivalent).

Recommendations

Let us close with a few recommendations:

- Board directors rarely have deep expertise in HR, organization development or psychology. Not all board members need to have HR expertise, but where none do, that is clearly a gap to be filled.

- Boards show less interest in broad workforce issues than they should; they have become tuned in to the idea of a deep leadership talent pool, but they need to get better at assessing whether people issues in the guts of the organization are hurting results or mortgaging the future.
- Analysts and investors often don’t understand the impact of better people management, so boards need to work on educating those key stakeholders.
- Boards are just beginning to be a role model for good HR practices. Boards need to show the employees that they care about performance, teamwork, selection and development by modeling best practices in their own work.

It is encouraging to see that human capital is on the agenda, but many organizations can still make significant improvements in how the board provides oversight on people-related issues, and thus help their management teams achieve lasting excellence.

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