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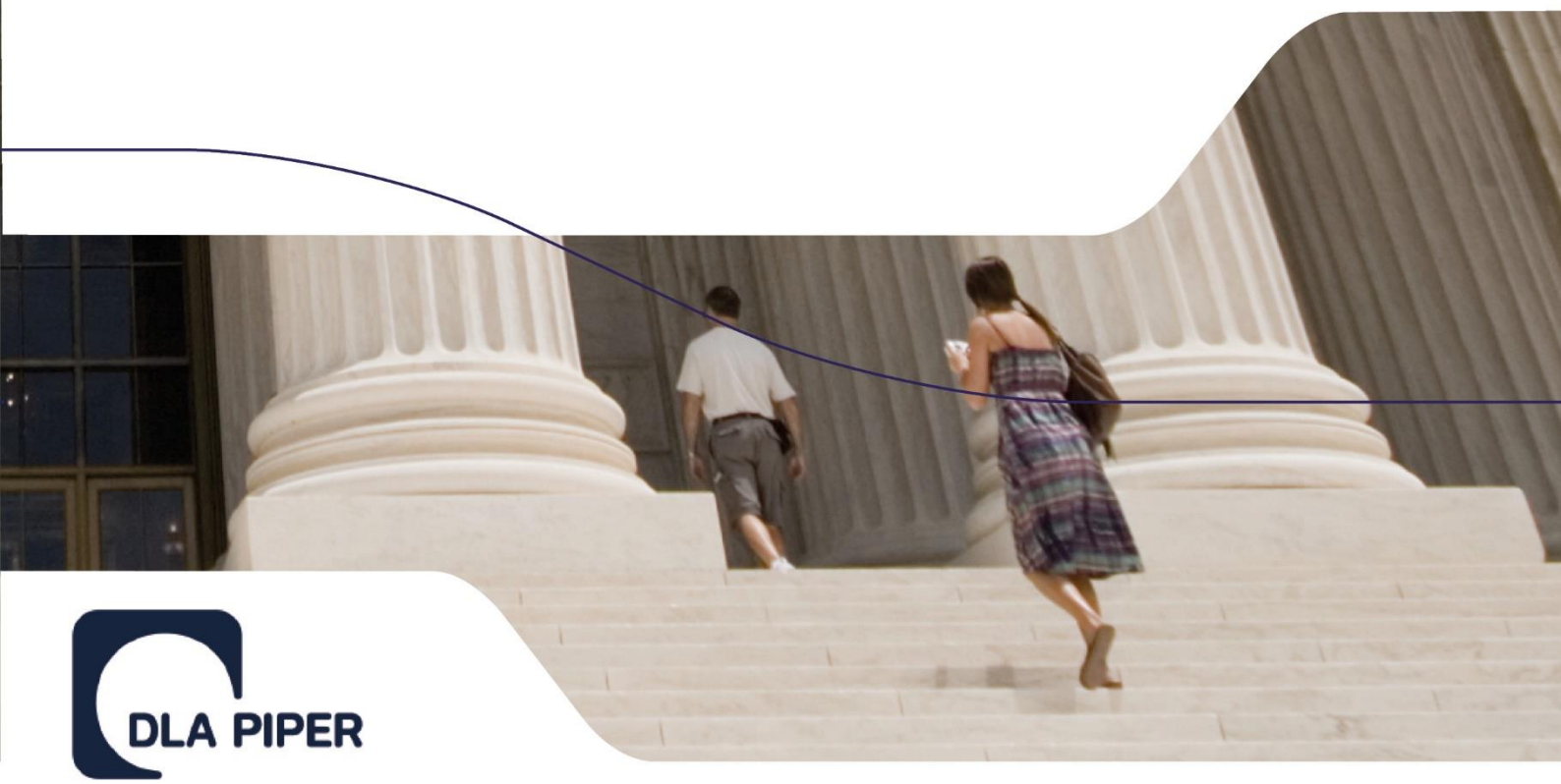
Technical Report

TRANSFORMATIONAL LEADERSHIP



Future of Boards
Phase 1: Part 3

Trends in board practice: Insights from our Initial Exploratory Research



DLA PIPER

The University of Cambridge Institute for Sustainability Leadership

CISL is an impact-led institute within the University of Cambridge that activates leadership globally to transform economies for people, nature and climate. Through its global network and hubs in Cambridge, Cape Town and Brussels, CISL works with leaders and innovators across business, finance and government to accelerate action for a sustainable future. Trusted since 1988 for its rigour and pioneering commitment to learning and collaboration, the Institute creates safe spaces to challenge and support those with the power to act.

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About the research

The Future of Boards Research Study by the University of Cambridge Institute for Sustainability Leadership (CISL), in partnership with the global law firm DLA Piper, explores key trends in how board practice and the wider legislative environment are changing around the world; how aligned with a sustainable future these trends in board practice, and their drivers, are likely to be; and the practical implications for boards.

We draw from primary and secondary data to understand trends and their drivers, and use a bespoke sustainability framework to understand whether or not these trends are likely to support, or be obstacles to, the alignment of business success with the long-term wellbeing of all people and planet. In other words, a sustainable future is understood as one where everyone's wellbeing is optimised, for which healthy social and environmental systems are required.

We are carrying out the research in two phases.

Phase 1 explores the evolving and emerging trends in board practices and capabilities, and the related legislative and regulatory context, using a range of primary and secondary data sources. This phase is divided into three parts.

Phase 1: Part 1 sets out the context, rationale and theoretical underpinning for this study, as well as the research design.

Phase 1: Part 2 explores the first domain of interest – trends in both 'hard' law (legislation and case law) as well as 'soft' law (such as codes of conduct and guidelines), which relate to areas of broad sustainability concern. This structured comparison of existing law enables us to gain insights into the legal context within which boards are currently operating, and are likely to operate, in the future. It also enables us to evaluate which trends, that are aligned with a sustainable future, warrant board support and leadership.

Phase 1: Part 3 is the focus of this report. It looks at three further domains which relate specifically to trends in board practice, and how these are operating in response to the evolving legislative context, and the wider pressures to achieve sustainability outcomes. These three domains are:

1) purpose, materiality, strategy and disclosure
2) board membership, structure, group dynamics, individual skills and capabilities
3) stakeholder engagement, including interfacing with investors.

Phase 1: Final Report: Summary and Synthesis includes insights from Part 1, 2, and 3 above.

Phase 2 of the research will explore and evaluate some of the findings from Phase 1 in greater detail. It will also arrive at a set of recommendations to enable boards to better align their organisations with sustainability outcomes, and positively contribute to a thriving future for all.

The research is being carried out with funding from, and in conjunction with, the global law firm DLA Piper, which is assisting CISL in identifying sources of data and gathering insights from multiple locations around the world. DLA Piper is also providing guidance and advice as the project progresses. It is important to note that while DLA Piper has funded this work, intellectual stewardship lies with CISL.

Background to the study and research framework

Rationale

Businesses, while providing one of the primary ways in which people's wants and needs are met, are also central to creating the grand challenges facing the world today, from climate change to biodiversity loss, or excessive inequalities in wealth, income and opportunity. These challenges also pose substantial risks for businesses.

Increasingly, business boards are under pressure, not only to respond effectively to these external risks, but also to understand and respond to stakeholder expectations, while remaining commercially viable in the short and long term. This situation is particularly challenging in the context of an increasingly tense and volatile global situation.

Within this rapidly evolving situation, difficult questions arise about the appropriate role and effective functioning of the board – as the key body (or bodies) responsible for the direction, oversight and accountability of an organisation.[1]

This research has been designed to offer practical support to boards in understanding, navigating and responding to the different observable trends in legal frameworks, board practice, board structure and stakeholder engagement that are facing them, and to evaluate the extent to which these are likely to impact on the ability of a board to align business success with sustainability outcomes. The full background to the research, as well as details of the methodology, can be found in the Phase 1: Part 1 report.

The research

Trends in board practice occur across many levels. On the basis of existing literature and insights, we are focusing on four areas, or 'domains'.

> For the purposes of this research, a **trend** is understood as the general direction in which something is developing or changing.

Domain 1 – Legal frameworks in a range of jurisdictions (both 'hard' law – legislation and case law, as well as 'soft' law – codes of conduct and guidelines) which shape and underpin board practice that directly relates to sustainability.

Domain 2 – Board practice, including purpose, materiality, strategy and reporting.

Domain 3 – Board membership, structure, individuals and dynamics.

Domain 4 – Stakeholder engagement (including investor interface).

We explore the trends in these domains through a combination of primary and secondary research, using multiple techniques – from questionnaires and interviews to literature reviews and analysis – to better understand these trends, their drivers, trajectory and pace of change. Although this governance challenge

affects all kinds of organisations, this research focuses primarily on large public or privately owned shareholder companies.

We also used a bespoke **sustainability framework** that enables us to explore the extent to which observed trends do or do not align with the long-term wellbeing of people and planet, by seeing how they map against three different business approaches to sustainability.

Table 1: Our sustainability framework

Approach to sustainability	Criteria
Corporate Social Responsibility (CSR)	• focus on short-term shareholder financial value maximisation • limited and unsystematic responses to societal and stakeholder pressure to limit negative environmental and social impacts. Action is based on relieving pressure from influential stakeholders and ultimately protecting short-term profit • strong rules-based and compliance mindset • primarily a self-interested motivation (short-term)
Enlightened Shareholder Value (ESV)	• aims to create long-term shareholder financial value • recognises the importance of operating within accepted environmental and social thresholds, and therefore natural, social and human capitals are stewarded, stock and flows of these capitals are accounted for, and benefits are allocated to ensure healthy stakeholders, including the environment • concerned with double materiality – external influences on financial income, and the impact of the organisation on the environment and wider society because of its impact on long-term financial performance (impact materiality) • varying levels of systemic response, from limited and partial (for example, targets for CO_2 emissions only), to explicitly aiming to operate within all accepted environmental and social thresholds (eg all Sustainable Development Goals, or all social and environmental elements outlined in *Doughnut Economics*)[2] • primarily a self-interested motivation (long-term)
Purpose driven	• has a clearly defined purpose which defines its reason to exist as an optimal strategic contribution to the equitable long-term wellbeing of people and planet • while all stakeholders are therefore the ultimate beneficiary, the organisational purpose acts as a strategic filter to direct all actions of

	the company towards an ambitious contributing aspect, or sub-stakeholder group • the purpose informs all value-creation goals and parameters for operating. These parameters ensure action within social norms and scientific consensus, and in a way that ensures the health of stakeholders, wider society and the environment, which is necessary to achieve the purpose, and/or may be the object of the purpose (as opposed to the reason to exist being to maximise financial value for members/shareholders) • the purpose is achieved within accepted environmental and social thresholds, and therefore natural, social and human capitals are stewarded, stock and flows of these capitals are accounted for, and benefits are allocated to ensure healthy stakeholders, including the environment • shareholders are seen as one of a number of core stakeholders, and profitability is seen as a vital means to achieve the purpose • primarily an externally directed 'other' orientation, with self-interest of the business as a means to that end (long-term)

Executive summary

Boardrooms are currently at an inflection point. The practical responsibilities of boards are rapidly evolving as a result of discussions about the purpose of business and the role of the board itself; competing stakeholder demands; and growing awareness of the interplay between financial viability, environmental, social and governance (ESG) risks and sustainability performance. These cumulative pressures are translating into changes in board practices across the three areas explored in this report:

- board membership, structure, group dynamics, individual skills and interpersonal capabilities
- purpose, materiality, strategy and reporting
- stakeholder engagement, including investors.

This changing landscape also contributes to a sense of excessive pressure on board members, arising partly from a mismatch between what is required of governance, and the availability of board time and expertise. Boards will need to identify more clearly their contribution to what are increasingly becoming existential threats to their business, as well as broader societal wellbeing, while reflecting on how they may need to change and adapt to be fit for the future.

In the area of board membership, structure, group dynamics, individual skills and interpersonal capabilities, we see a number of clear shifts.

Board membership is undergoing change as evidence indicates a slow increase in the overall diversity of the board. Our findings show the following trends:

- The number of board directors from countries other than that in which a company is headquartered (as one measure of cultural diversity) is static globally, but varies by geography and sector.
- There are gradually increasing numbers of strictly independent non-executive directors (NEDs) as a proportion of the board.
- The number of people sitting on boards internationally is static at around nine, although varying from six to 11 geographically.
- In the case of board tenure, data indicates a relative stability at around seven years, with some geographical variability.
- There are increasing numbers of women on boards, but the rate of increase is slow and there is wide geographical variation.
- Representation of ethnic minorities on the boards of publicly listed companies is increasing, albeit at a slow rate and from a low base.

Board structure is under scrutiny as designing appropriate board structures becomes increasingly important:

- Data shows a relatively rapid increase in the number of sustainability-related sub-committees among listed companies. However, the extent to which these sub-committees are adopted varies significantly across geographic regions and industrial sectors. Furthermore, concerns have been raised regarding their effectiveness in driving sustainability practices.
- Nomination sub-committees are showing a gradual and steady global increase among listed companies, starting from an already high baseline. However, there is significant variation in the levels of nomination sub-committees based on geographic regions.
- Audit committees are being consistently maintained at a high level globally, except for Latin America where the presence of audit committees is relatively lower.

Board dynamics are being recognised as a crucial aspect of effective governance, one which is also reflected in what appears to be increasing numbers of board evaluations:

- There are indications that some boards are slowly evolving to become more independent, inclusive and collegiate, although this trend appears to be culturally and geographically variable.
- There is a slowly rising number of companies having a written policy and/or practical intention concerning the independence of their boards.

Nevertheless, board independence extends beyond mere formal status. It is also a mindset characterised by a willingness to challenge business-as-usual, ask difficult questions, and be willing to confront engrained norms, power dynamics and assumptions:

- Aligned with the growing emphasis on board independence, there is also an increasing trend towards separating the roles of the chair and CEO.
- Simultaneously, the presence of CEOs on boards is slightly decreasing.
- Our findings also suggest that the skills of the board chair are emerging as a key driver in shaping and influencing board dynamics.

Individual skills and interpersonal capabilities required in boardrooms are also undergoing change:

- There is increasing attention on the need for a wider range of technical skills and knowledge on boards, as well as growing appreciation of more inclusive and relational leadership capabilities.
- However, there are also concerns that these additional skills and enhanced capabilities are not being realised in practice to any great extent.
- Evidence also indicates a rising demand for capabilities that transcend traditional business or financial expertise.

These shifts in requirements suggest a growing need to refresh the board by recruiting new board members who bring a wider range of skills that can effectively respond to the evolving needs of the

organisation, and by developing and upskilling existing board members. Among these evolving dynamics, the role of the board chair is again of utmost importance.

In the areas of purpose, materiality, strategy, reporting and stakeholder engagement, there are discernible shifts in outlook, but also considerable variability in how these shifts are realised in practice.

Purpose, materiality, strategy and disclosure

Evidence indicates that there is an increasing focus on organisational purpose at board level, but its realisation is clouded by confusion over how it is understood; how to create a board–management consensus; and how to translate it into operational priorities and organisational change. However, it is also evident that purpose has not yet had a systematic influence on strategy, exposing a disconnect between the discussions around purpose and its effective integration into strategy formulation and decision-making.

Boards are, however, displaying a growing commitment to strategic engagement, albeit starting from a relatively low baseline. There are additional indications of the greater inclusion of sustainability issues within board discussions. However, the predominant approach continues to revolve around information provision and acquisition, indicating room for further progress.

Furthermore, boards are increasingly using materiality assessments and engaging in related discussions, although it is difficult to identify any move towards using 'double' or 'impact materiality', away from 'single', or even just 'financial materiality'. In addition, the influence of board-level materiality assessments on strategy appears limited.

Lastly, there are slowly emerging signs that some boards are beginning to view ESG (and integrated) reporting not merely as compliance requirements but as integral components of overall strategy development. This recognition signifies a gradual shift towards acknowledging the strategic value of sustainability reporting for business goals.

Stakeholder engagement is slowly evolving:

- Boards are demonstrating a consistent and intense commitment to engage with shareholders and investors, and with indications of increased shareholder relations beyond annual general meetings (AGMs).
- There are also signs of increasing tension between boards and some institutional shareholders within publicly listed companies, adding another layer of complexity to the dynamics of corporate governance.
- There is growing discussion by boards around the benefits, and most appropriate ways, of engaging stakeholders.
- There is an increase in stated corporate stakeholder engagement, although practical implementation remains largely centred on financial stakeholders, primarily shareholders.

Overall, there are encouraging signs of innovation in how the boards of some companies are engaging with non-financial stakeholders, reflecting an evolving landscape of board engagement strategies.

Further research is needed to identify more detailed insights into how these observed shifts in board practice (for example, around diversity, independence, the role of the sustainability committee, strategy development, materiality analysis and reporting) are actually enabling long-term sustainable value creation for companies and wider society, and will help build an evidence base for action.

Further insight is also needed into the contextual elements that shape how these trends play out in different businesses, ranging from industrial sectors, ownership structures and company size, to culture and geography. The trends in this report have largely been identified at a global aggregate level, yet early findings suggest that they vary across different geographies and jurisdictions.

Phase 2 of this research will therefore provide further insights into selected key areas of board practice across a range of contexts, and provide practical recommendations for boards looking to be fit for the future.

Results in detail and implications for board practice

Table 2: Big picture trends affecting boards

Big picture trends affecting boards	
Big picture trends affecting boards	**Implications for board practice**
Growing emphasis on ESG has impacts on boards and regulatory compliance.	• Boards are increasingly expected to engage with and oversee ESG risks, and embrace new opportunities for the business. • There is a need for boards to ensure robust ESG reporting and disclosure practices and to establish appropriate metrics, monitoring frameworks and third-party audit systems. • Boards may require reassessments of their own composition and capabilities to ensure effective oversight. • Boards are likely to benefit from moving from a compliance mindset to proactive board leadership on ESG performance.
Increased cumulative pressure on board practice resulting from complex and diverse external pressures, and increased areas of board oversight.	• To make best use of limited time, boards should be focused on staying abreast of macro trends capable of impacting on the business and on social and environmental wellbeing. • Boards will need to direct their energy towards mid- and long-term time horizons as well as focusing on short-term survival. • Boards may need to increase the number of board members; create more specialised board structures; and search for more diverse skills among directors to secure access to expertise in emerging areas (for example, in technology, sustainability, or risk management). • Boards will require more comprehensive monitoring and control mechanisms, clear reporting lines, effective data collection and streamlined information flows on material issues.

Enhanced role of the board and scope of governance.	• Boards will need to move away from a narrow focus on financial risks towards a greater acknowledgement of the interplay between financial viability and sustainability risks. • The increase in the practical responsibilities of boards goes along with a need to shift from being reactive to more proactive board leadership of the company. • Boards need to balance and negotiate increasing – and sometimes contradictory – stakeholder demands. • There needs to be enhanced collaboration between management and external stakeholders, but also proactive management to reduce friction when board activities encroach on those of executive management. • Boards need to acknowledge and creatively address the mismatch between what is required of governance and the availability of board time. • There needs to be more focus on the evaluation of board performance.

Table 3: Board composition and membership

BOARD COMPOSITION AND MEMBERSHIP		
Trends	**Further insights**	**Implications for board practice**
Trend 1: Increasing board diversity		
Evidence of a slow increase in the overall diversity of the board. However, trends vary by geography, and different demographics (for example gender or ethnicity) are progressing at varying speeds. It also appears that far less attention is being paid to other aspects of diversity such as cultural and cognitive diversity, mental and physical disability, age or experience.	There is a well-established trend towards increasing numbers of women on boards, but the rate is slow and there is wide geographic variation. Data on the global ethnic diversity of boards is difficult to find or interpret. However, there seems to be evidence of a trend towards increased representation of ethnic minorities on boards, albeit at a slow rate and from a low base. There are also indications of a recent acceleration in some geographies.	• Boards may find greater diversity to be a safeguard against 'groupthink', bringing diversity of perspective and thought to decision-making. • Boards should reframe diversity away from tokenistic quota-filling to seeing it as a strategic resource to be leveraged for more effective oversight and decision-making. • Boards will need to consider broader diversity criteria (eg culture, age, class, experience), as well as diversifying their sources of information, and the ways of thinking, underlying board decisions. • Board members may experience greater risk of interpersonal challenges, less cohesive collaboration and slower decision-making as a result of such changing dynamics. • The importance of the role of board chair becomes even greater with enhanced diversity, in mediating competing perspectives and enabling inclusive decision-making.
Trend 2: Increasing numbers of strictly independent non-executive directors		

There is a trend towards gradually increasing numbers of strictly independent non-executive directors (NEDs) as a proportion of the board. 'Strictly independent' NEDs are defined here through their fulfilment of a set of rigorous criteria, identified by the Refinitiv Eikon Global Companies Database. These criteria include having no direct personal or financial links with the company, and not owning more than 5 per cent of the company's shares.	The number of people sitting on boards internationally is static at around nine, although varying from six to 11 geographically. Board tenure shows relative stability at around seven years, but with some geographical variability.	• Board independence is widely accepted as a benchmark of good corporate governance, enabling more constructive board dynamics and less risk of groupthink. • Boards need, however, to ensure that independence is not merely a formal status but a 'habit of mind', which enables people to probe key assumptions or the usual way to do things. • Boards should also foster a sense of belonging and psychological safety to enable board members to support and challenge each other. • In order to ensure appropriate independence, there is a need to manage potential 'over-boarding' (people sitting on too many boards at the same time). • Boards need to be aware that independence on boards depends on nomination policy, which may mean that nomination decisions may be influenced by powerful shareholders.

Table 4: Board structures

BOARD STRUCTURES		
Trends	**Further insights**	**Implications for board practice**
Trend 3: Increasing discussion of appropriate board structures, with an increase in sustainability-related sub-committees		
There seems to be growing debate about how to structure boards and sub-committees, with a trend towards increasing numbers of sustainability-related sub-committees, albeit with some concern expressed over their effectiveness.	Sustainability-related sub-committees appear to be on a fairly rapid rise among listed companies, although with different levels geographically and across sectors. Nomination sub-committees are increasing globally at a slow rate, from a high base, but with significant variation in levels geographically. Audit committees are at a high and steady level globally, except in Latin America where the level is relatively lower.	• Boards will need to create adaptable board structures that are responsive to the evolving landscape. • Boards should also recognise the potential governance benefits arising from knowledge specialisation, stronger diligence and board accountability, as well as the benefits of restructuring boards in order to free up time for more strategic engagement. • There is, however, a need for boards to recognise the risk of specialist sub-committees impairing communication flows, and creating silos and decision bottlenecks. • Such sub-committees require clear committee-level mandates to embed sustainability considerations into broader organisational structures and processes. • The outputs of such sub-committees should be integrated into board decision-making and company strategy. • In addition to a clear mandate, the sub-committee needs to have an appropriate composition to ensure maximum-impact succession plans and working procedures, as well as ensure that guidelines enable cross-committee collaboration.

		• Boards will also need to be aware that there is ongoing debate about where compliance and reporting should sit within the organisation and how it should report up to the board without conflicting advice, for example, via the finance, legal, or sustainability functions – all of which could be conflicted.

Table 5: Board dynamics

BOARD DYNAMICS		
Trends	**Further insights**	**Implications for board practice**
Trend 4: Increasing attention being paid to board dynamics and board evaluations		
There is growing awareness of the importance of board dynamics, which is also reflected in what appears to be increasing numbers of board evaluations. There are indications that some boards are slowly evolving to become more inclusive and independent, although this trend appears to be culturally and geographically variable.	There is a slowly rising number of companies having a written policy and/or practical intention concerning the independence of their boards. The roles of chair and CEO are increasingly separate. The presence of the CEO on boards is decreasing slightly. There are indications that board evaluations are slowly increasing around the world at different rates, although their quality is variable.	• By increasing attention on board dynamics, boards will need to recognise that this focus also spotlights power dynamics, authority bias, groupthink, confirmation bias and sticking to the status quo. • Additionally, board independence is not merely determined by the number of NEDs but by the actual behaviours and actions of board members. • Boards should consider doing evaluations which include consideration and improvement of board dynamics and culture, enabling the diffusion of best governance practices and sound decision-making. • Evaluations can also enable a greater focus on what counts as performance, and assessment of the desired objectives against which effectiveness is evaluated.

	There is a shift from hierarchy to collegiality on the board. There is greater recognition of the importance of group dynamics for realising the potential of board diversity. The skills of the chair are important for board effectiveness. Board evaluations are increasingly focused on board dynamics.	• Boards will need to recognise that it can be difficult to nurture thoughtful board dynamics in the face of immediate pressures and increased complexity. • There is therefore greater scrutiny of, and expectations of, board chairs as catalysts of constructive board culture, dynamics and decision making. • Relatedly, boards need to transition from just representing diversity to leveraging diverse backgrounds, mindsets and perspectives to invigorate board dynamics, and with the steer of the chair ensuring that everyone is heard, and sound decisions are made.

Table 6: Individual skills and interpersonal capabilities

INDIVIDUAL SKILLS AND INTERPERSONAL CAPABILITIES		
Trends	**Insights**	**Implications for board practice**
Trend 5: Increasing desirability of wider technical skills and knowledge, and more human and collegiate leadership skills		
There is increasing attention being paid to the need for a wider range of technical skills and knowledge on boards, as well as growing appreciation of more inclusive and relational leadership capabilities. However, there are also concerns that these additional skills and enhanced capabilities are not being realised in practice to any great extent.	The increasing desirability of a wider set of technical skills and knowledge beyond those of traditional business or finance. There is also a growing appreciation for leadership skills that reflect the (changing) role and purpose of boards. There is more attention being paid to the capabilities required to create constructive group dynamics, particularly with regard to the chair. Skills and knowledge requirements reflect the changing role and purpose of boards, and the need to refresh the board by recruiting new members who bring a wider set of skills and capacities, as well as provide training and upskilling to existing members.	• Boards will need to ensure that they are well rounded and composed of directors with cross-cutting skills complemented by expert development, as well as advice from specialists in relevant fields. • Boards will also need to recognise the importance of ensuring that individuals with complementary skills generate self-reinforcing group dynamics which boost cohesiveness and foster collaboration. • There is also a need for boards to encourage collaborative mindsets and cultivate cohesive board dynamics to unlock the full potential of diverse perspectives and skills. • Boards can create a pipeline and succession plan of diverse talent to nurture future board members with diverse skill sets.

Table 7: Summary of key insights about purpose, materiality, strategy and disclosure

Summary of key insights about purpose, materiality, strategy and disclosure	
Insights	**Implications for board practice**
There is increasing discussion around purpose at board level, but with some confusion over how it is understood, and limited evidence that it is systematically driving strategy.	• Boards should ensure that they clearly understand the different approaches to sustainability (CSR, ESV, Purpose driven), and the drivers for, and practical implications of, these approaches. • Boards will also need to shift their temporal outlook from a narrow focus on short-term gains to longer-term imperatives. • Additionally, boards will need to recognise that the areas of non-financial risk oversight are expanding; and ensure that their strategic focus includes value drivers that go beyond financial return. • A focus on purpose can lead to invigorated board-level dynamics by accommodating a broader representation of investor, workforce, societal and consumer perspectives within boardroom decision-making.
There is an increase in strategic engagement by boards, and indications of more integration of sustainability issues and purpose. The general approach is, however, through information provision and acquisition.	• Boards should become more involved in strategic engagement, strategic planning, and the consideration of the risks and opportunities involved in strategy formulation and the metrics which they prioritise for evaluating success. • To enable this greater focus on strategic priorities, there is a need for boards to consider systematically how they balance their priorities within limited board time.
There is an increase in the use of and discussion about materiality assessments by boards. However, any move towards using 'double' or more 'impact materiality', away from 'single' or just 'financial materiality' is harder to assess.	• Boards should see materiality assessments as part of a suite of analytic assets to inform strategy and balance short-term gains and long-term sustainability. Prudent businesses should also be considering scenario analysis and other forms of forward-looking modelling. • Materiality assessments also make visible the trade-offs involved in decision-making and their impact on stakeholders, and might influence capital allocation if boards decide to mitigate potentially disruptive risks at the expense of short-term gains.

At the moment that shift, and its influence on strategy, appears limited.	• Boards will need to ensure more targeted and proactive stakeholder engagement and analysis of future trends, using for example scenario analysis, to inform materiality assessments. • Boards should recognise that a more focused attention on materiality can catalyse the re-evaluation of corporate success, spotlight new value drivers, and revise the appropriate metrics of corporate performance. It might even prompt the rethinking of business models to unlock hidden commercial opportunities arising from sustainability. • Boards will, however, also need to be aware of and consider conflicting approaches to materiality in mandatory standards, when they are determining their approach to materiality.
There is some indication that boards are slowly seeing ESG (and integrated) reporting, and the data acquisition underpinning it, as part of overall strategy development, not just a compliance requirement.	• Boards will need to recognise that achieving progress on a particular sustainability metric may require resource reallocation, re-engineering business processes, revising internal procedures, re-designing employment roles, or even undertaking a broader organisational overhaul. • Boards will also need to consider where compliance and reporting should best sit within the organisation for maximum effect, and how the organisation should report to the board without conflicting advice, for example, from the finance, legal, or sustainability functions. • In order to ensure adequate data collection, the use of data methodology due diligence, internal control and governance, and third-party assurance systems, may need to be ensured by the board. • To carry out this role, boards will need to consider the need for capacity-building and new pools of expertise, or even new board structures to oversee non-financial reporting. • Boards will also need to recognise that potential legal or reputational liabilities arise from green- or purpose-washing, cherry-picking, box-ticking and tokenism.

Table 8: Summary of key insights around stakeholder engagement

Summary of key insights around stakeholder engagement	
Insights	**Implications for board practice**

There is a stable and high level of intent by boards to engage with shareholders and wider investors, with indications of an increase in shareholder relations beyond AGMs. However, there is also evidence of tension emerging between boards and some categories of shareholders.	• Boards should be careful about prioritising board-level engagement with shareholders over other stakeholders, since this may erode trust and support from non-financial stakeholders with potential risks arising from activism, which can expose businesses to litigation and reputational risk. • Boards will also need to maintain good relationships between the board and investors in order to avoid board attention being diverted away from their core governance responsibilities and increasing the risk of proxy battles and shareholder activism.
There is a growing narrative by boards around the benefits and most appropriate ways to engage stakeholders, as well as an increase in stated corporate stakeholder engagement. It appears, however, that practice remains dominated by engagement with financial stakeholders.	• Boards will need to clarify the division of labour with regard to stakeholder engagement between management and boards. • Boards will need to be aware of the influence of proxy advisors and how to navigate this. • Boards should also recognise that multi-stakeholder engagement can spark innovation by identifying unseen operational inefficiencies, unmet customer needs and untapped markets. • Stakeholder engagement also plays a crucial function in materiality assessments and sustainability reporting, both as sources of input and as monitoring agents. • There is also a risk of stakeholders politicising boards, as different stakeholder groups try to influence corporate decisions to support their preferences. • Boards should avoid appeasing multiple constituencies with contradictory demands and interests since this might lead to intractable trade-offs.
There are slow and emergent signs of increasing innovation in how boards engage with non-financial stakeholders.	• Boards will likely benefit from developing innovative methods to engage with a wide range of stakeholders to foster synergies between them, allowing boards to leverage partnerships, anticipate change and amplify their impact in multiple ways.

1. Introduction

The previous report covered Phase 1: Part 2 of the Future of Boards research initiative. It focused on the legal and regulatory environment affecting the evolving context within which boards are operating around the world.

This report (Phase 1: Part 3) shifts the focus to trends in how boards themselves are operating in practice, and the behaviour of board members.

It covers three broad areas:

- Domain 2: board practice, including purpose, materiality, strategy and reporting
- Domain 3: board membership, structure, individuals and dynamics
- Domain 4: stakeholder engagement (including investor interface).

There are three distinct features of this report, which differ from the approach taken in Phase 1: Part 2.

First, in Phase 1: Part 2, we focused on changes in legislation and regulation that specifically related to broad sustainability considerations across a diverse sample of jurisdictions. In this report, we instead take a wider view, and focus on general trends in board practice and operations, rather than just those that primarily focus on sustainability. We have, however, been careful to focus on areas of changing board practice. In other words, we have not focused on trends that represent a continuation of dynamics that have tended to characterise board practice for the last couple of decades. As such, many of those trends that we have identified represent a shift from what we might refer to as a 'business-as-usual' position, which is discussed further in Section 1.2 below.

The scope of enquiry in Part 3 still remains wide. For this reason, the findings at this stage are high-level and indicative. The aim is to identify early insights, tentative trends, and areas which are worthy of further detailed exploration in Phase 2 of the research project.

Second, due to the wide scope of the work and time constraints, we have prioritised data sources from our own primary data collection and one particular source of secondary data (which are summarised below). We also made limited, selective use of further secondary data sources to triangulate the insights from the primary data sources, providing supporting detail or nuance. This material is presented in shaded text boxes throughout the report. These summaries do not provide comprehensive coverage at this stage. A deeper and broader analysis of secondary data sources will be carried out in Phase 2 to explore chosen areas of interest in more detail.

Third, the three domains addressed in this report are reported with different degrees of depth. The coverage and analysis of Domain 3 is deeper than that for 2 and 4 as a result of its relatively clear and narrow scope, and the greater level of in-depth responses in our interviews. It has therefore been possible to identify both trends, and more indicative insights across the various topics covered in this domain, as well as offer some tentative reflections on alignment with sustainability outcomes.

1.1. Methodology

The three main sources of information, a Global Trends Survey we carried out, expert interviews, and the Refinitiv Eikon Global Companies Database, are detailed in Phase 1: Part 1 and summarised below.

1.1.1. The Global Trends Survey

The Global Trends Survey is a short overview survey. It was created as an initial, broad-brush scan of the landscape of trends in board practice, including both quantitative and qualitative questions. It was prepared and distributed to individual executive and non-executive board members, as well as to people who have an interest in boards, such as advisors. (Further details of the respondent characteristics, as well as results from the survey, can be found in Appendix 1.)

Potential respondents were identified, and accessed, through LinkedIn, CISL and DLA Piper networks. Of the 433 responses completed between May and October 2022, 331 were valid (in other words, all relevant questions were completed) and could be included in further analysis. Respondents lived in 61 countries around the world.

The respondents were heavily weighted towards Europe (particularly the UK). They were also likely to be biased towards being pro-sustainability as a result of the way in which they were recruited. The results are therefore not comprehensive enough to draw globally valid conclusions at this stage of the research. Rather, they provide an initial scoping of possible broad trends. Despite the geographical bias, the results do have wider validity since they are likely to be signals of the direction of wider change.

1.1.2. Results of expert interviews

We interviewed 29 individual experts, and held two group workshops between CISL and DLA Piper representatives, between August 2022 and January 2023, with one further interview conducted in June 2023 to address a gap in coverage of the domains being researched. The methodology for the analysis of the data can be found in Phase 1: Part 1.

The interviewees were selected as those people who were likely to have significant knowledge of the wider landscape from which to be able to provide broad insights into existing and emerging trends. They were identified through a combination of professional networks across a range of jurisdictions, desktop research, and the Global Trends Survey. They covered most of the globe (see Appendix 2 for interviewee characteristics and coverage). The interviewees were generally independent consultants, or those based in organisations, covering areas such as governance, compliance, reputation, environmental, social and governance (ESG) board behaviour, and stakeholder engagement. There were also several representatives from finance, and non-governmental organisations (NGOs). The two group conversations were held between CISL and DLA Piper to reflect on the emerging findings. Details of how the interviews were transcribed and analysed can be found in Part 1.

Although respondents were asked to consider the full breadth of trends in board practice, given the initial framing of the study, the reputation of CISL as a sustainability institute, and the networks from which respondents were drawn, interviewees may have filtered some of their responses (consciously or unconsciously) through a sustainability lens. However, the interview guide encouraged broad reflection. The responses received indicate that the people interviewed were aware of a wide range of trends, and their associated drivers, as well as their practical implications and challenges.

Quotes from the 29 interviews are found indented and in italics, accompanied by a reference number that corresponds to the interviewee summary found in Appendix 2.

1.1.3. The Refinitiv Eikon Global Companies Database

The Refinitiv Eikon Global Companies Database tracks over 450 ESG metrics from around 10,000 of the world's largest quoted companies (typically those with a value of more than US$400 million) across 76 countries. The information is gathered from companies' annual reports, sustainability reports, stock exchange filings, and other news and third-party commentary. This information is pooled to create a comprehensive ESG dataset on each company. While the limitations of ESG ratings are acknowledged and have been explored,[3] Refinitiv is understood to be one of the few providers that gives transparency around its data quality assurance methodology.[4] With this in mind, and given the size and scale of the dataset, it is one of the most promising tools to identify macro trends at a global level. At the time of data collection, the data was available in full from 2017 to 2021, and with partial indicative data from 2022. The data is also broken down by both geography and sector (Appendix 3).

The database has a global reach but is restricted to large publicly listed companies. It therefore cannot identify trends which are occurring in privately owned businesses, or those which are publicly owned but smaller in size.

1.2. Analytical approach

As outlined in **Phase 1: Part 1**, and summarised at the beginning of this report, the research team has adopted a simple framework to create an initial assessment of the alignment of the observed trends and insights with sustainability outcomes. This framework is based on work already undertaken by CISL.[5]

The three stylised logics, Corporate Social Responsibility (CSR); Enlightened Shareholder Value (ESV); and Purpose driven, are summarised in Table 1 in the previous section in this report on Background to the study and research framework. They articulate three different approaches to sustainability. In this simple way of dividing up logics, we see each of these approaches relative to 'business-as-usual' (BAU).

BAU, in the way we are using this phrase (with the details and implications set out in Table 9, is not meant to be an accurate depiction of the current business environment and all the different motivations and practices of companies, but rather highlights a way of thinking about business that has been particularly influential. As such it can help to explain some of the constraints and drivers which perpetuate certain motivations, and activities which may conflict with achieving positive sustainability outcomes.

The origins of this particular conception of BAU can be found in neoliberal economic thinking and practice developed by thinkers such as Friedrich A Hayek, building on earlier neo-classical 'laissez-faire' economics which underpinned early capitalism.[6] Milton Friedman's work was particularly influential in embedding and extending these principles to influence business behaviour, as well as the supportive external ecosystem (or reinforcing culture and practices of finance, business norms and government policy). His famous 1970 article in *The New York Times*, which summarised this position, included the oft-quoted statement that: "there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits".[7]

While the origins of this thinking, and resultant practice, arose primarily in the US, as well as the UK, the influence of this particular BAU has become embedded in business school teaching, as well as in the

international norms of business and finance practice.[8] While businesses around the world operate within different cultures and legal systems, and within different 'varieties of capitalism', this particular kind of BAU has had a pervasive international influence, particularly on the largest and publicly listed companies.

Table 9 sets out some of the resulting assumptions which underpin BAU. This summary was developed by CISL in a 2021 publication *Unleashing the Sustainable Business* by Victoria Hurth and Aris Vrettos.[9]

Table 9: The core assumptions underpinning BAU organisational logic

Assumption	
Self-interest	Humans are best understood as primarily motivated by self-interest. This self-interest drives optimal market effectiveness and maximises the positive outcomes of the economic system. Managers are assumed to generally maximise their own interests, which may or may not coincide with the interests of shareholders.
Profit maximising/ utility maximising	Humans' self-interest is primarily to maximise their 'utility', a proxy for welfare/wellbeing, and to achieve this in an economy by buying goods and services. Companies' self-interest is to maximise profit, which maximises the utility and income of shareholders.
Theory of rational behaviour (or bounded rationality)	Individuals are rational and make decisions to maximise their utility/self-interest.
Shareholder primacy	Shareholders are the rightful beneficiary of company action (the 'principal'). Governing bodies and managers are 'agents' acting on behalf of shareholders to maximise the latter's interests, that of profit.
Competition	Competition between companies is believed to keep organisational self-interest in check by ensuring that they pass on sufficient value to customers rather than retain it for themselves.
Minimised government intervention and spending	A perfectly running, free market does not need government intervention and is the best way to allocate resources in society. Where market failures exist (monopolistic power, information asymmetries, or the failure of markets to price in externalities) government intervention may be justified (although the extent of acceptance of market failures varies among neoliberal thinkers).
Perfect information	If everyone in a market has complete (perfect) information, then the market will run at maximum efficiency and without the need for government intervention.
Values and responsibilities neutral	Acting on social values in a business context reduces freedom and imposes one person's views on another. A business cannot have values and responsibilities, only a person can. The appropriate way for these personal

	values to be expressed is through democratic governmental processes. The expression of personal values in business decisions (other than by shareholders) comprises an abuse of the resources entrusted to managers for the purposes of profit maximisation.
Freedom of consumer choice	The greater the choice, the more likely someone is to be able to fulfil their particular routes to wellbeing (utility). Constraining choice, for example, through business-initiated choice-editing, if not for profit-maximising, is anti-market and amounts to imposing a company's values on the consumers' ability to maximise their own utility.
Value is subjective to the individual. The customer is king (consumer sovereignty)	What is of value (utility) to an individual is entirely subjective, yet it is also stable and knowable through market transactions.
The rationale for consumer preferences is not the concern of the company	It is not necessary to understand what underpins consumer preferences to deliver what consumers want. Preferences are revealed through consumer choice in the market via the products and services they demand. This intelligence is best achieved by market research. Consumers are 'rationally self-interested utility maximisers' and so they know best how to optimise their own utility. Therefore, a company should concentrate on its own self-interest and let consumers focus on theirs. Any attempt to educate consumers, or otherwise alter preferences, is a distortion of the market.
Trickle down	Wealth is created through innovation and entrepreneurship, which should be incentivised since the results benefit those on low incomes: 'a rising tide lifts all boats'.
Private property	People and companies should be free to own material and non-material possessions (eg intellectual property) that others (particularly the state) cannot take from them.
Globalisation (economic)	The concept of a free market is a global one and not confined to arbitrary national borders. National barriers to trade (protectionism) enforced by governments therefore reduce global wellbeing outcomes, as they constrain the potential for the market to meet consumer preferences as efficiently as possible.
Limits on physical resources will be solved through innovation or price signals/substitution	Resource constraint problems can be overcome through innovation and/or pricing, limiting demand in line with supply constraints. Hence, there are no formal limits on resources that need to be considered by organisations. There is likely to be a natural limit to environmental degradation when incomes reach a certain level and people begin to demand higher environmental standards (known as the 'environmental Kuznets curve').
Growth is a sign of success	The success of an organisation or individual is only constrained by their abilities and effectiveness to deliver what others require (which is

	underpinned by self-interest). If a person is very rich, or a company extremely large, this is because they are doing a good job in delivering utility. Such success is to be welcomed as long as it is achieved within the rules of the game, and not to the exclusion of fair competition.
Short-termism (a consequence of the above assumption in practice)	This is not an objective but an outcome of a system in which shareholders demand profit maximisation. As stocks are commoditised, investors move fast to find the greatest and least risky returns. This creates momentum towards the prioritisation of short-term performance.

As a BAU way of thinking has been so influential in shaping business and its associated governance practices for the last few decades, many of the trends in changing board practice that we have identified through this research are likely to represent a potential shift from a BAU position. Our analytical approach makes this explicit, using the three stylised logics of Corporate Social Responsibility (CSR), Enlightened Shareholder Value (ESV) and Purpose driven as a mechanism for positioning these changes and emerging trends relative to how far they represent a shift from a BAU position.

1.3. Structure of the report

This report first covers some of the most salient trends and insights emerging from the views of our expert interviewees. It then covers several cross-cutting themes in more detail, before moving on to discuss each of the three domains of inquiry in turn.

The first domain to be discussed is Domain 3, covering the structure and make-up of boards, since this area attracted the most responses, and makes particular use of hard data from the Refinitiv Eikon Global Database. It includes some initial reflections on the sustainability implications of the trends.

Findings from Domains 2 and 4 which follow are more tentative, and presented as insights rather than trends, since they cover large and rapidly changing areas.

The report ends with a section on conclusions which uses the sustainability framework to assess the extent to which these trends and insights are moving towards a fully sustainable business future.

2. Big picture trends and pressures affecting boards

The experts we interviewed were asked, through open-ended questions and without specific prompts, to articulate what they observed as leading trends relating to changing board practice. While most of these are dealt with in detail in Sections 3 and 4, others reflect not necessarily trends but ongoing systemic issues that cut across and affect the more specific trends we explore in detail below in this section.

The most commonly mentioned cross-cutting theme, by over two-thirds of our expert interviewees, related to the impacts of ESG on the board (which seemed from the responses to the interviews to often be used interchangeably with the wider notion of sustainability), particularly in relation to the need for reporting, and compliance with new legislation and regulations.

Sustainability is a concept that describes, in the words of the international standard ISO 37000, "a state of the global system, including environmental, social and economic aspects, in which the needs of the present are met without compromising the ability of future generations to meet their own needs".[10] Applied to a business context, it is a mindset for conducting business, concerned with the interdependency between a company and the wider environment and society in which it operates.[11]

ESG is a non-reporting financial framework, providing a measured assessment of sustainability using benchmarks and metrics. Although it has a long history,[12] it is commonly now used to describe a framework developed for evaluating the sustainability-related disclosure of listed companies for investors.[13] It is sometimes referred to as the financialisation of sustainability, as part of a general trend towards sustainability accounting.[14]

Both 'sustainability' and 'ESG' have weaker and stronger interpretations leading to more conservative and radical implications respectively. We set out our understanding of 'sustainability' in particular in Part 1, which provides the underpinning foundations for our analysis of the trends identified in this research.[15] We acknowledge, however, that other sources in this report (eg expert interviews, secondary data) – may use 'sustainability' and 'ESG' in different ways and often as synonyms to refer to the general agenda of businesses' relationship with wider social, environmental and governance issues.

The next most important issue facing boards, raised by over half of the interviewees, was the complexity and perceived increase in external pressures (arising from, for example, geopolitical risks, digital and cybersecurity, artificial intelligence (AI), cost of living). This trend was frequently summarised as that of operating within a VUCA (volatile, uncertain, complex and ambiguous) environment.[16]

Two further areas which arose repeatedly in both the Global Trends Survey and expert interviews were:

- an enhanced (but also unclear) role of the board
- the related widening and changing ideas around the scope of governance.

Each of these is now briefly discussed in turn, with reference to further selected secondary data.

2.1. ESG and sustainability

The area of ESG and sustainability cuts across all the issues covered in Domains 2, 3 and 4, and as such is a constant thread throughout this report. A particularly salient insight to make at this point, however, which arose from both the Global Trends Survey and the interviews with experts, was the virtual lack of mention of any other environmental issue than climate across both the survey and the interviews. There were only occasional references to, for example, biodiversity, or a circular economy. There were also relatively few mentions of the social dimensions of sustainability beyond diversity.

Annual conferences hosted by some of the main corporate governance institutes internationally are a useful way to indicate emergent trends. It is notable that across several of the major institutions, a recurrent central topic of interest – more so than any other theme over the last 3–5 years – has been the integration of ESG and sustainability concerns into governance. For instance, the Global Corporate Governance Colloquium has included key sessions around the implications of ESG for the board for the last six years,[17] while the Chartered Governance Institute annual conference has included agenda items relating to ESG for the last three years at least.[18] In a similar vein, the Global Network of Director Institutes (GNDI) virtual conference in 2022 headlined key themes around ESG, sustainability, social inclusion and climate change.[19] The Asian Corporate Governance Association annual conference likewise has featured ESG and sustainability trends as the key topic of discussion for the last three years, with a specific focus on how this trend plays out in the particular cultural contexts of Asia.[20]

The *Global Network of Director Institutes 2020–2021 Survey Report* in collaboration with Marsh McLennan analyses survey responses from over 2,000 directors worldwide on the theme of board governance during the COVID-19 crisis.[21] In the wake of the pandemic, the survey reported that 67 per cent of respondents felt that an increased focus on ESG, sustainability, and stakeholder values was one of the most likely long-term trends impacted by COVID, second only to a predicted trend around incorporating the expertise of outside experts into scenario planning and strategy and risk decision-making processes.

Expert interviewees felt that *"the climate crisis is very front of mind"* for boards and that this was increasingly being seen as a *"principal risk".* A 'net zero' plan was even suggested by one interviewee to be a must-have. You need *"to have a net zero plan because your competitors have". (15)*

Another interviewee, a reputation consultant based in the UK, felt that ESG and sustainability were becoming more central to the board's concerns*:*

> *"…successfully [integrated] alongside the traditional oversights that they've had. So, I think it's quick. I'd say it's really accelerating." (6)*

However, while it was clear from our research that there is more awareness that the board's practices are being affected substantially by sustainability issues, some boards and board members still do not think that sustainability is part of their role.

One sustainability consultant felt that he rather sees:

> *"…a mix of appetite among board members about how much they want to get into [sustainability]. Some not so much. They don't see it as really their role … And I would say it's still quite divided. You*

still have some people who [say] very firmly: 'We look at the financials and that's our role as stewards', whereas other people do see a broader role." (20)

2.2. External and complex pressures on boards

The operating context for many boards is characterised by a number of external factors that are both complex and volatile. These include, but are not limited to the effects of COVID-19, rising energy costs, the unpredictable macro-economic climate, the speed of innovation, the cost of living crisis, digital and tech changes (including cybersecurity and AI), geopolitical risk, as well as the practical implications of changing climatic conditions. This operating context has a potentially significant impact on both board time in terms of the sheer number of issues to consider and board decision-making, arising from the complexity inherent in many decisions.

It appears overall from the interview responses that board members feel as though they are being constantly bombarded with a range of external issues, and hence potentially overwhelmed.

One interviewee summed up this position:

"…there is a polycrisis going on … layers of crisis which are environmental, climatic, social and economic but also increasingly political or geopolitical … a kind of perfect storm … which is brewing outside. I think most of the boards and organisations I'm seeing, and working with, are detecting that. What they're doing about it, I think, is a different question … I think they're struggling. I think they are really struggling to say, how do we handle this complexity as a board?" (7)

Moreover, board experts from other sources agree that, particularly amplified by the pandemic, there are more decisions for boards to make with more uncertainties and higher stakes, within a shorter time period.[22]

Advice and training are increasingly available for equipping boards and their members in VUCA contexts to balance more effectively short-term and long-term decisions,[23] make high-consequence decisions quickly and in ways that improve performance,[24] and build resilience in terms of how businesses anticipate, adapt, and/or resist adversity.[25]

2.3. Enhanced but uncertain role of the board

There was an overall view that, at a fundamental level, the board was taking its role more seriously, as well as being more professional and accountable for the actions and activities of the company.

However, at the same time, interviewees felt that there was:

- an unclear position regarding the role of the board versus that of executive management in relation to different issues
- a lack of clarity about the role of the board within wider governance structures and processes
- a lack of time to take on new roles and responsibilities.

2.3.1. Enhanced role for the board

"They're taking it very seriously … The level of professionalism … around the world is increasing … What would have been acceptable 20 years ago, 10 years ago, even 5 years ago is no longer acceptable." (22)

Russell Reynolds Associates observed in their 2022 Global and Regional Trends in Corporate Governance study, a trend towards enhanced board effectiveness being the norm as investors and other stakeholders realise that good composition, refreshment and evaluation practices result in improved corporate performance and decreased risk exposure.[26] In 2023, the review suggests this year will see further scrutiny of board quality, effectiveness and composition, with experienced and empowered stakeholders paying close attention to many aspects of board performance, and increased efforts to make board evaluation processes more rigorous.[27]

The pandemic was felt by some respondents to be a particular driver, both of greater reflection by boards about their role, as well as requiring boards to practically respond differently or more frequently than they might have previously.

Another interviewee suggested that, at a more substantive level, there had been a shift in focus towards addressing:

"…more systemic risks … [being] more future oriented … [with] less [time spent] on oversight and control." (8)

However, a corporate governance training provider, based in the Caribbean, did not see such a clear move, but rather a mixed picture:

"I still see that we continue to have some boards which are hands off almost to the point of just rubber stamping, and there are some boards where the directors are beginning to question if this is the right way, and what their role really is supposed to be." (13)

It also appears, from the perceptions of our expert interviewees, that boards are spending more time on ESG and sustainability issues, as well as on other external pressures, rather than just looking at the financial and purely commercial aspects of a company's operations.

"In general, boards are spending much more time than they used to on what used to be called the soft issues … That means in essence … shifting away from spending all of their time looking at finances and the commercial aspects of the business, to looking at issues around the external context, particularly in terms of socio-political shifts and threats, the regulatory environment." (7)

2.3.2. The role of the board within wider governance

Two-thirds of interviewees spoke in terms of the importance of considering the wider structure and processes of governance within which the board sits. It was felt that this factor is an important aspect in any consideration of board trends, or of the role of the board, since boards are embedded within, and an integral part of, different aspects of wider governance.

As a governance training provider said:

> *"We still haven't had that fundamental shifting in our thinking of what governance really means." (13)*

Despite the scope of what needs to be governed being articulated and extended through the various international corporate governance and stewardship codes and legislation we considered in **Phase 1: Part 2**, the evolving situation according to a governance consultant based in the UK:

> *"…is still embryonic in terms of are we even asking the right questions and what are good practices, what are best practices and they are changing over time … we just didn't have language [before] like stewardship [of] sustainability." (22)*

A positive step, however, to begin to bring together and anchor this changing scope of governance, and within that the role of the board, was seen by several interviewees to be the development of standards, particularly ISO 37000, which is the standard used as the basis to define governance in this research.[28] As one corporate governance academic and practitioner pointed out:

> *"When I start to challenge the board about its leadership and governance capabilities, it's useful to have a framework to call upon." (7)*

The international standard, *ISO 37000: 2021 Governance of organizations – Guidance*, sees the governance of an organisation as being:

"a human-based system by which an organization is directed, overseen and held accountable for achieving its defined organizational purpose. At its core this includes:

a) setting and committing to the organizational purpose and organizational values;

b) determining the organization's approach to value generation;

c) directing and engaging with strategy to generate value;

d) overseeing that the organization performs and behaves according to the expectations set by the governing body;

e) demonstrating accountability for this performance and behaviour."

It is worth noting, however, that these expert insights are likely to play out differently in different sectors and organisation structures. For instance, respondents also referred to the importance of recognising how the practicalities of governance, and what is appropriate or possible, can differ according to the stage of development of companies, or the sector. For example, in relation to the IT industry, one reputation consultant reported:

> *"…it's quite interesting seeing these companies literally growing at pace and struggling with their governance … a lot of these quite high-profile companies, which have grown very fast – consumer brands and B2B brands … have had well publicised issues with their governance … very major negative repercussions, which can take a long time to recover from." (28)*

There were also suggestions that the kind of people who set up companies, such as entrepreneurs in certain sectors such as technology, may be resistant to any form of formal governance processes, and particularly to influence from external members of boards. With reference to such entrepreneurs, another reputation consultant commented:

> *"They're going to rail against a highly structured world where you need to have a board that looks like this. And they don't want to work like that … It comes down to the people in the end … Do you want an open discussion at the board? Do you want to be challenged about what could go wrong? Do you really want that, or do you basically want people to rubber stamp what you've already decided to do? … Inevitably powerful people … [are] more used to getting their own way. They don't really want challenge." (27)*

The scope and role of board responsibilities and oversight, within the wider governance framework, is clearly being affected, to different extents, by the changing legislative and regulatory environments that we are seeing across the world, and which were set out in Phase 1: Part 2. However, this pressure affects different kinds of companies to different extents:

> *"I'm not sure that it is actually finding its way in to change systems and processes just yet … For the listed companies, I think they invest a lot in ensuring that the directors are able to fulfil these kinds of roles. But the private organisations, I think not so much yet." (13)*

2.3.3. The role of the board vis-à-vis executive management

Many of the comments raised by interviewees suggested a lack of clarity over whether many of the issues raised in Domains 2 and 4 are believed by board members to be part of their remit, rather than that primarily of executive management. Even if it is clear to a board that responsibility for a particular area lies with them, the question remains: 'What is their exact role (vis-à-vis the executive)?' For example, is it to oversee the processes by which something happens, sign off on a completed action, provide constructive thoughts and criticism, or be directly involved in strategic decision-making and information-gathering, and if so, in what way (for example, in partnership with management, or independently)?

It also appears from our interviewees that any shift towards greater empowerment and responsibilities of the board can potentially create difficulties with executives who have been used to maintaining control over, for example, strategy or reporting:

> *"They [the board] come once a quarter. They're not involved in the day-to-day operations, but they want to come and tell me how I need to run my business." (10)*

On the other hand, the rise in complexity and scope of decision-making has meant that some boards are working more closely and intensely with the management team:

> *"[The board] have to meet more frequently and to understand their role in being able to be sounding boards, and to provide guidance to their management team." (13)*

2.4. More intensive and changing work practices

> *"It's … more challenging because actually companies are demanding much more time from their board members…" (8)*

These changing and often additional responsibilities mentioned above also come up against the challenge of time. For example, with regard to all the current issues facing global companies:

> *"It's frankly impossible for the board, per se, to do that, but they clearly have to authorize and empower competent people, competent specialists … on their behalf." And, even if the board has a*

clear role, it still may have to be "delegated to those who can, who can focus on the details of issues." (27)

This time pressure, as well as the practicalities of COVID, seemed, from our interviewees, to have resulted in boards shifting to different and more intensive ways of working, with the use of more online meetings rather than just face-to-face, as well as increased time commitment by board members.

The amount of work has also led, exacerbated by COVID, to more board work being undertaken online, a:

"…move to virtual … and in-person board meetings as well as hybrid." (20)

In the wake of COVID-19, Russell Reynolds Associates identified the shift to virtual board and shareholder meetings as a key trend in its 2021 annual review of Global and Regional Trends in Corporate Governance, as many boards seek to leverage the associated efficiencies post-pandemic.[29] Based on their experience of working with hundreds of public company boards around the world every year, Russell Reynolds notes that many boards will develop a hybrid calendar where at least one meeting per year remains virtual and many ad hoc and committee meetings stay online.

The increasing time required by board members seems to have also led to concern about over-boarding (sitting on too many boards at the same time) and the challenge this creates in relation to the increased expectations of board members regarding their engagement and participation:

"One of the big things here is the work commitment that individuals are expected to do. As a result of that they're on fewer boards … They've got to devote more time to each and every board that they're on. They're expected to be a lot more professional in terms of what they're doing, and how they're managing things." (22)

"…non executive directors have a limited amount of time … the range of things they're supposed to know about, or interrogate, grows ever longer by the day." (27)

The Global Board Survey 2021, published by Intersearch, based on 1,782 responses from 79 different countries and legal jurisdictions, reported that the workload of boards continues to increase. This trend has been apparent since 2014, with 66 per cent of respondents putting in more hours preparing for and participating in board meetings. This reflects a trend towards moving closer to the business and daily management.[30] The *Global Network of Director Institutes 2020–2021 Survey Report* similarly revealed that two-thirds of the about 2,000 director respondents reported that over the past year their board time commitment increased by 50 per cent or more.[31] This figure reflects the fact that in the months after the COVID-19 crisis broke, board governance became more intense and more frequent. More recent data suggests that this trend is continuing, with a Spencer Stuart Pulse Survey of 743 public and private directors revealing that nearly 75 per cent perceived a slight or significant increase in time obligations over their tenure.[32]

2.5. Big picture trends and pressures affecting boards: concluding reflections

The following section draws together the emerging key trends, reflects on their potential meaning for board practice, and tentatively suggests implications for business sustainability using the lens of the three logics of business-as-usual (BAU) Corporate Social Responsibility (CSR), Enlightened Shareholder Value (ESV) and Purpose driven.

2.5.1. Interim conclusions on big picture trends affecting boards

Boardrooms are currently at an inflection point. The challenge of governing increasingly complex companies, which are also facing a range of equally complex and diverse external pressures, is compounded by the effects of expanding areas of board oversight; enhanced public accountability; intensifying regulatory scrutiny; as well as increased and sometimes conflicting stakeholder expectations. As we found in Phase 1: Part 2, while the legal duties of boards are relatively unchanged (although evidence shows that they are starting to shift, for example, in supply chain due diligence requirements) – although themselves increasingly contested – the practical responsibilities of boards are rapidly evolving as a result of discussions about the purpose of business and the role of the board itself; competing stakeholder demands; and growing awareness of the interplay between financial viability, ESG risks and sustainability performance.

These cumulative pressures are translating into changes in board practices across the three domains that we explore in this report. They also contribute to a sense of excessive pressure on board members, arising partly from a mismatch between what is required of governance, and the availability of board time. Boards will also need to identify more clearly their contribution to what are increasingly becoming existential threats to their business, as well as broader societal wellbeing, while reflecting on the ways in which they may need to change and adapt to be fit for the future.

2.5.2. Implications of big picture trends affecting boards for business sustainability

The expert interviews identified a range of responses to the VUCA context in which many businesses are operating. There was an overall perception that the resultant cumulative and volatile pressures have led to some companies responding with a focus on short-term survival and ongoing financial viability, therefore squeezing out both short and longer-term sustainability considerations.

> *"Companies and directors are really trying, in the short term to … survive. And so there's been a push away from … the integration of sustainability, that we've seen … [They] are currently being squeezed … in terms of their margins … First it was COVID, and now they've moved into a period with … rising prices and everything else that's happening in our world. I think that's really shifted the pendulum back to … [a] relentless focus on profit." (21)*

> *"I think the external noise is particularly amplified at the moment. There are so many crazy things that are going on in the world, that it's still difficult to get positioning for sustainability." (15)*

In other cases, however, interviewees spoke about the role of the board in resisting this pressure to respond in short-term and reactive ways, instead retaining a strategic focus:

> *"It's the role of the board, it seems to me, to remain above the daily hubbub of business to see the mega trends and to … persuade the executive to consider new ways of doing things that may be very unfamiliar and even uncomfortable, but which are necessary if you're serious about tackling really difficult sustainability problems." (7)*

This suggested approach does not mean that maintaining such a strategic focus is easy. With limited time and capacity on boards, as well as the additional pressures of a changing world, the tendency to behave in a short-term way is likely to affect even those businesses which are firmly committed to pursuing long-term and strategic wellbeing goals. In fact, as a governance expert based in Brazil said:

"To boards of directors that take long term impact decisions, this [situation] is even more challenging." (5)

Businesses will respond to the pressures of complex and volatile external pressures in different ways. We can use our three organisational approaches (business-as-usual CSR; ESV; and Purpose-driven approach) to analyse the different responses that businesses might make if they are predominantly adopting one of these logics:

- Business-as-usual CSR approach. The particular demands of VUCA provide further impetus to focus exclusively on short-term profit maximisation.
- ESV approach. There could be a deliberate effort to integrate longer-term strategic considerations into decisions about immediate operational challenges, which also creates a more agile and adaptive response to ongoing change.
- Purpose-driven approach. Unity by the board and senior management around purpose could provide a clear sense of direction and decision-making framework within which to navigate the VUCA environment, along with greater clarity around the decisions that sit with the board, those that sit with the executive, and those that need to be collective.

This sustainability analysis is not to suggest, however, that an ESV or Purpose-driven logic would remove, or even reduce, the weight of responsibility and sense of pressure currently felt by boards. Rather, both the ESV and the Purpose-driven approach could equip boards (particularly the Purpose-driven logic) with a clear sense of their role and responsibilities, a broader and more strategic perspective, and a decision-making framework for making high-level and fundamental decisions about the future direction and operations of the company.

3. Board membership, structure, dynamics and skills

The first domain of board practice to be discussed is that of board membership, structure, dynamics and skills (this is what we referred to as Domain 3 in our original research design) or what has become known as the 'black box' of how boards actually function. This domain seeks to identify emerging trends in relation to who sits on boards; how these individuals behave and inter-relate; and how boards organise themselves in order to address different issues.

We are therefore looking specifically in this section at the people themselves (their demographics, background, experience, skills and capabilities); formal board structures (such as sub-committees), as well as the emergent 'personalities' and dynamics of boards that arise from their collective interactions.

This 'black box' has been identified as a key area in need of further research.

A recent paper by Tayan and Larcker (2023) published in the Harvard Law School Forum on Corporate Governance, identifies seven 'gaping holes' in our knowledge of corporate governance. The first is around 'board effectiveness' and understanding what attributes (composition, structure or practices) make a board effective, despite "a mountain of research". The authors conclude that the vast majority of research into 'structural' attributes – such as CEO/chair duality, board tenure, diversity, busy directors, board size, director age, professional qualifications, active or retired CEOs – finds that most of these attributes are not associated or only loosely associated with actual outcomes (with the possible exception of busy boards, which appear to be an impediment to board effectiveness). The authors reflect that a more promising area of study is to understand the practices that make for effective board leadership, including the qualities of the individuals who direct the board. Very little careful study has been made of the differences in board leadership across companies, and whether effective board leaders share common backgrounds, skills, or approaches.[33]

We mostly use insights from our experts, with the addition of empirical data from the Refinitiv Eikon Global Companies Database, where this is available. Supplementary insights are provided by the Global Trends Survey, and selected additional secondary data sources.

More specifically, we look at four thematic areas of interest:

1) **Board composition and membership** – the demographics (for example, gender and ethnicity), status (for example, executive or non-executive), board size and length of board tenure.
2) **Board structures** – how boards are structured, including the use of sub-committees.
3) **Board dynamics** – the culture and relationships between board members.
4) **Individual skills and interpersonal capabilities** – specific areas of expertise and experience, as well as broader leadership capabilities.

In addition to identifying trends, we also offer some tentative reflections on the extent to which they do or do not align with positive sustainability outcomes. At the end of the report, we pull these reflections together into a more substantive discussion – explored through the lens of the three 'logics' in our bespoke sustainability framework – and which create early interim conclusions for the research project.

For each area, high-level trends and associated sub-trends are first highlighted. Each trend and sub-trend is then discussed using supporting data (from expert interviews, the Refinitiv Eikon database and selected secondary data sources) to inform the main drivers, likely trajectories, and observed challenges and counter-trends.

3.1. Summary of trends

Section 3.2: Board composition and membership

Trend 1: Increasing board diversity (Section 3.2.1)

There is evidence of a slow increase in the overall diversity of the board. However, trends vary by geography, and different demographics (for example, gender or ethnicity) are progressing at varying speeds.

It also appears that far less attention is being paid to other aspects of diversity such as cultural and cognitive diversity, mental and physical disability, age or experience.

Sub-trends:

- There is a well-established trend towards increasing numbers of women on boards, but the rate is slow, and there is wide geographical variation.
- Data on the global ethnic diversity of boards is difficult to find or interpret. However, there seems to be evidence of a trend towards increased representation of ethnic minorities on boards, albeit slow, and from a low base. There are also indications of a recent acceleration in some geographies.
- The number of board directors from countries other than that in which a company is headquartered (as one measure of cultural diversity) is static globally, but varies by geography and sector.

Trend 2: Increasing numbers of strictly independent non-executive directors (Section 3.2.2)

There is a trend towards gradually increasing numbers of strictly independent non-executive directors (NEDs) as a proportion of the board.

'Strictly independent' NEDs are defined here through their fulfilment of a set of rigorous criteria, identified by the Refinitiv Eikon Global Companies Database. These criteria include having no direct personal or financial links with the company, and not owning more than 5 per cent of the company's shares.[34]

Further insights:

- The number of people sitting on boards internationally is static at around nine, although varying from six to 11 geographically.
- Board tenure shows relative stability at around seven years, but with some geographical variability.

Section 3.3: Board structures

Trend 3: Increasing discussion of appropriate board structures, with an increase in sustainability-related sub-committees (Section 3.3.1)

There seems to be growing debate about how to structure boards and sub-committees, with a trend towards increasing numbers of sustainability-related sub-committees, albeit with some concern expressed over their effectiveness.

Sub-trends:

- Sustainability-related sub-committees appear to be on a fairly rapid rise among listed companies, although with different levels geographically and across sectors.
- Nomination sub-committees are increasing globally at a slow rate, from a high base, but with significant variation in levels geographically.
- Audit committees are at a high and steady level globally, except in Latin America where the level is relatively lower.

Section 3.4: Board dynamics

Trend 4: Increasing attention being paid to board dynamics and board evaluations (Section 3.4.1)

There is growing awareness of the importance of board dynamics, which is also reflected in what appears to be increasing numbers of board evaluations. There are indications that some boards are slowly evolving to become more inclusive and independent, although this trend appears to be culturally and geographically variable.

Sub-trends:

- There is a slowly rising number of companies having a written policy and/or practical intention concerning the independence of their boards.
- The roles of chair and CEO are increasingly separate.
- The presence of the CEO on boards is decreasing slightly.
- There are indications that board evaluations are slowly increasing around the world at different rates, although their quality is variable.

Further insights:

- There is a shift from hierarchy to collegiality on the board.
- There is recognition of the importance of group dynamics for realising the potential of board diversity.
- The skills of the chair are important for board effectiveness.
- Board evaluations are increasingly focused on board dynamics.

Section 3.5: Individual skills and interpersonal capabilities on boards

Trend 5: Increasing desirability of wider technical skills and knowledge, and more human and collegiate leadership skills (Section 3.5.1)

There is increasing attention being paid to the need for a wider range of technical skills and knowledge on boards, as well as growing appreciation of more inclusive and relational leadership capabilities. However, there are also concerns that these additional skills and enhanced capabilities are not being realised in practice to any great extent.

Further insights:

- There is an increasing desirability of a wider set of technical skills and knowledge beyond those of traditional business or finance.
- There is a growing appreciation for leaderships skills that reflect the (changing) role and purpose of boards.
- There is a growing appreciation of the 'human' side of leadership.
- The acknowledgement of the importance of capabilities relating to creating constructive group dynamics, particularly with regard to the chair.
- The skills and knowledge requirements reflect the changing role and purpose of boards.
- The need to refresh the board by recruiting new members who bring a wider set of skills and capacities, and provide training and upskilling to existing members.

3.2. Board composition and membership

The first thematic area explored as part of this domain is that of board composition and membership. This section looks at trends in the diversity of the people who sit on boards. The focus, due to the available data, is primarily on their demographic characteristics (such as gender, ethnicity, or cultural background); or status (whether they are executive or non-executive directors (NEDs)). We look at these two aspects separately in Section 3.2.1 on increasing board diversity, and in Section 3.2.2 on strictly independent non-executive directors.

This section also includes a short analysis of board size and board tenure (Section 3.2.3) since these aspects both potentially relate to the ability of a board to realise the benefits of its diversity and independence.

Overlapping trends around the implications of this enhanced diversity for board dynamics are explored in Section 3.4, and what this means for individual skills and interpersonal capabilities, in Section 3.5.

3.2.1. Trend 1: Increasing board diversity

There is evidence of a slow increase in the overall diversity of the board. However, trends vary by geography, and different demographics (for example, gender or ethnicity) are progressing at varying speeds.

It also appears that far less attention is being paid to other aspects of diversity such as cultural and cognitive diversity, mental and physical disability, age or experience.

In the Global Trends Survey, one of the key themes emerging in response to the question: "What do you believe to be the most significant trends affecting board practice today?", was that of board composition and board diversity.

Over half of the expert interviewees also talked about a perceived trend towards greater board diversity.

"We've come a long way from boards being made up of friends of the chair or CEO." (27)

Interviewees also recognised, however, that different dimensions are changing at different speeds, and that these vary across different geographies and contexts. A more rapid increase in gender diversity, and a slower increase in ethnic representation, were the most frequently mentioned sub-trends. Summarising the different responses, there was an overall view from interviewees who referenced board diversity, that gender parity and appropriately representative ethnicity, despite these increases, has not been achieved, and still requires substantial work. Additionally, it was felt that it is still early days for a full consideration of different types of diversity, for example, ethnicity, neurodiversity, age, disabilities, intellectual diversity, sexuality, class or family income background.

> *"I think [diversity] is a trend that has momentum, but I don't see it changing at a really rapid pace or that we're anywhere near some of the targets and aspirations that have* [been] *put in place by various reports in the past. It still seems to be relatively slow going from that point of view." (6)*

A contribution to the Harvard Law School Forum on Corporate Governance by Russell Reynolds Associates about their work on 2021 Global and Regional Trends in Corporate Governance notes a growing interest in diversity and inclusion. In 2020, comments made by global investors and corporate governance professionals suggested a trend towards a more expansive view of board diversity beyond gender, that includes race and ethnicity.[35] In 2021, this trend had accelerated, especially in the US, at the level of the board, C-suite and employees. There were also increased investor demands for disclosure of key data on diversity, equity and inclusion.[36]

Other literature, however, suggests that this concern for board diversity is not necessarily reflected by support at the level of individual board members.

PwC's 2019 Annual Corporate Directors Survey suggested that support for board diversity is fading after climbing steadily for years. They note a nearly ten-point drop since 2018 in the percentage of directors saying that diversity is very important on their boards. The percentage talking about racial/ethnic diversity fell from 34 per cent to 26 per cent, and age diversity fell from 21 per cent to 14 per cent.[37] In the same survey, 83 per cent of directors, including more than 50 per cent of female directors, said they do not support laws mandating gender board diversity, such as those passed by California.

In the 2022 version of the survey (with 704 respondents), the findings show that while directors still see clear benefits in board diversity, there continues to be growing unease. For instance, the number agreeing that increased diversity enhances company performance dropped from 76 per cent in 2019 to 73 per cent in 2022. A growing number are also more likely to say that efforts to diversify boards result in unneeded candidates (34 per cent, up from 27 per cent in 2019) and almost one-third of directors (31 per cent) said that the push for diversity is resulting in unqualified candidates – up from just 23 per cent three years ago.[38]

Geographical variation in diversity trends is likely to be particularly influenced by issues such as cultural norms, political drivers, and legal and regulatory requirements.

In order to further investigate these perceptions about diversity in board composition from the expert interviewees, we used the Refinitiv Eikon database to indicate specific sub-trends over time, by geography and by sector. As previously outlined, the database covers large publicly listed companies across 76 countries, so the following information can only give a broad indication of trends among a subset of boards. The Refinitiv Eikon data also does not fully operationalise the idea of 'diversity'. It is restricted to

selected demographic characteristics, namely: gender equality, ethnic diversity, and a particular dimension of 'cultural diversity' – the percentage of board members who are not from the country in which the business is headquartered.

3.2.1.1. Board diversity sub-trend: gender equality is slowly increasing

There is a well-established trend towards increasing numbers of women on boards, but the rate is slow, and there is wide geographical variation.

Table 10: Percentage of women directors sitting on boards (2017–21)

	2017	2018	2019	2020	2021	2022
% women directors	15.9	18.0	19.3	20.9	22.7	(23.8)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

Refinitiv Eikon's data shows an increase from 15.9 per cent of directors who are women in 2017, to 22.8 per cent in 2021 (and provisionally to 24.9 per cent in 2022). Overall, around one in four global directors are women. There are wide geographical variations, ranging from the lowest in Latin America and the Caribbean (12.6 per cent in 2021), to the highest in Africa (27.5 per cent) and in Europe (27.5 per cent).

There are no stand-out differences across industrial sectors, except a relatively lower level in 'Energy' (16.6 per cent in 2021).

Several interviewees felt that a move towards increased gender parity was the dominant diversity trend:

> *"Boards have been already in the past decade taking steps [towards greater gender diversity] that I think in the past five years have accelerated." (8)*

Even so, however, additional data sources drew attention to the need for continued and further progress. This is particularly important given parallel concern about 'over-boarding', people sitting on too many boards at the same time (see Section 2.4 on More intensive and changing work practices), which can be a particular problem for women since the pool is even smaller than that for men.

The United Nations Global Compact has warned that the increase in gender diversity on boards is "alarmingly slow",[39] despite the presence of quotas in some countries, such as the EU.[40]

Deloitte's regular Women in the Boardroom survey provides one of the most comprehensive grey literature studies. It similarly agrees that the rate of change is at a "snail's pace".[41] The seventh edition, published in early 2022 (using 2021 data) found that, of 10,493 companies analysed, with a combined 176,340 directors, there was only a proportion of around 19.7 per cent female directors. This is up by just 2.8 per cent from its last survey in 2019. They calculated that if this rate of increase persists, it will take until 2045 to achieve boardroom equality.

Looking at board chairs, the numbers are even lower. The Deloitte study found only 6.7 per cent women, rising from 5.3 per cent in 2019. This percentage is slightly higher than that of female CEOs at 5 per cent in 2021, and 4.4 per cent in 2019.

The geographical variation observed in our data is also supported by other studies. According to the Deloitte data, France has the highest female representation at 42 per cent. However, some countries have fewer than one in ten female directors, such as in the Gulf. Qatar, for example, only has 1.2 per cent. In the UK (for those companies registered on the FTSE), annual data from recruiter Spencer Stuart shows that for the largest 150 FTSE companies, 39 per cent of directors are women, and 13 per cent are chairs, a dramatic rise from 15 per cent and 1 per cent respectively ten years ago.[42]

3.2.1.2. Board diversity sub-trend: ethnic diversity

Data on the global ethnic diversity of boards is difficult to find or interpret. However, there seems to be evidence of a trend towards increased representation of ethnic minorities on boards, albeit slow, and from a low base. There are also indications of a recent acceleration in some geographies.

The consultancy firm McKinsey & Company has monitored ethnic diversity in boards, executive teams, and within business more widely, since 2014. Following a cohort of around 1,000 large companies in 15 countries, their latest study in 2020 reports that progress towards ethnic diversity is slow in the boardroom, among leadership teams, and in companies generally. One dataset shows an increase from 14 per cent to 19 per cent representation of ethnic minorities in board positions between 2014 and 2019, with another dataset showing an increase from 14 per cent to 16 per cent between 2017 and 2019.[43] There is also significant variation between companies.

This slow pace of change is supported in a 2021 study on *Board Diversity and Effectiveness in FTSE 350 Companies* by the UK's Financial Reporting Council in conjunction with London Business School. They show that 59 per cent of FTSE 350 boards did not have a single ethnic minority background director in 2020.[44]

A 2020 McKinsey report, *Diversity wins: How inclusion matters*, shows that those companies in the top quartile of ethnic diversity (in general) outperformed those in the bottom quartile by 36 per cent in terms of profitability – a conclusion which reinforces the report's concern about the slowness of the trend towards increasing ethnic diversity.[45]

There is some evidence, however, that the pace of change may be accelerating in various parts of the world. The board diversity study by headhunter Spencer Stuart found that, in the US S&P 500 company index, almost half – 47 per cent – of new directors are from minority racial and ethnic groups, including Black/African American, Asian, Hispanic/Latino/a, American Indian/Alaska native or multiracial.[46] Other research found that one-third (33 per cent) of all new independent directors are Black/African American, three times more than in 2020 (11 per cent).[47]

These statistics were reflected in comments from the interviewees. For example, one interviewee, while noting the slow gender pace of change, felt that:

> *"…ethnic diversity is quite a distance behind. And if you start to think about … neurodiversity … I think that's still a way down the track." (28)*

Table 11: Percentage of ethnic minority board directors (2017–21)

	2017	2018	2019	2020	2021	2022
% ethnic minority directors	n/a	n/a	n/a	22.8	22.4	(23.4)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

In terms of the Refinitiv Eikon database, insights are more limited. Data is only available for 2020 and 2021 for most regions of the world (except Oceania) so therefore cannot indicate global trends.[48] It shows that the percentage of board directors with an ethnically diverse background (identified as the "percentage of board members classified under racial/ethnicity minority groups" in that country) is around 22.6 per cent. Indeed, the fact that data is only collected from 2020 is an important point in itself, indicating the relatively recent attention being paid to this agenda.

Geographically the data is quite spread. In 2021, Africa showed 50.2 per cent ethnic minority representation, with the UK the lowest at 15.6 per cent. However, these statistics are particularly difficult to interpret since they are likely to be contextual. The numbers depend on how 'ethnic minority' is defined, and their extent relative to the group which is determined to be 'dominant', presumably in the countries in which the companies are headquartered.

Across sectors, the Refinitiv Eikon data shows no real differences.

3.2.1.3. Board diversity sub-trend: number of foreign directors on boards is static

The number of board directors from countries other than that in which a company is headquartered (which is one measure of cultural diversity) is static globally, but varies by geography and sector.

Table 12: Percentage of foreign directors on boards (2017–21)

	2017	2018	2019	2020	2021	2022
% directors with cultural background different from that of the company's HQ	25.8	26.1	26.0	26.0	25.2	(21**)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers **Percentage data here could only be accessed at whole number level

One, albeit limited, measure of cultural diversity is whether or not board members come from different countries from the one in which the company is headquartered. The Refinitiv Eikon data in Table 13 shows

a fairly consistent trend. Around a quarter of all board directors are from 'other' backgrounds over the past five years, with a possible recent decline.

This relative stasis holds across all regions but with evidence of geographical variation in level. In 2021, the lowest rate is 15.2 per cent in Oceania, and the highest, 29.8 per cent in Europe.

Sectors also show variation with the lowest in 'Real Estate' (17.9 per cent in 2021). The highest in 'Energy', at (36.9 per cent), is also the sector in which there is the lowest ethnic minority score.

Evidence from Spencer Stuart tracks 'foreign' directors among its 150 FTSE companies. Their data shows that the percentage of 'foreign directors' is fairly static, at 34 per cent in 2012, and 35 per cent in 2022. However, the number of boards with either at least one foreign NED, one foreign executive director and/or one foreign director declined over this period, suggesting that this trend is variable across companies.[49]

3.2.1.4. Drivers of board diversity

Having identified a number of trends and sub-trends regarding board composition and membership, we now turn to exploring potential drivers for increased diversity, as suggested by the interviewees. These were the changing legal and regulatory environment; equity considerations; and the recognition of the benefits of diversity for creating an effective board.

The impact of the legal and regulatory environment has already been explored within Phase 1: Part 2. Diversity-related provisions, including targets, quotas and disclosure requirements, are increasingly found in corporate governance codes, listing rules and legislative acts across the world.

Focusing on equity, a number of interviewees highlighted increasing public sentiment and associated societal expectations regarding diversity being the right and equitable thing to do.

> *"Our institutions need to better reflect society, and I think we're going to see that in the boardroom." (21)*

In the US, but also in other countries influenced by the same or similar movements, the Black Lives Matter (BLM) movement is an example of public pressure that seems to have acted as a significant driver to improve ethnic diversity on boards.

> *"You know George Floyd, and Black Lives Matter was a very material accelerant … the degree to which the conversation has changed around big corporates in particular, in terms of racial diversity has changed dramatically." (27)*

There is also increasing acknowledgement that board diversity is important because of the recognition of the benefits of increased thought or experience diversity as an important part of creating a board with more effective decision-making.[50,51] While there were no Refinitiv Eikon data points available on the age of board members, a clear sentiment was expressed by a number of interviewees that younger board members may be able to bring a fresh perspective, and perhaps would be more likely to be focused on diversity and sustainability issues, as well as using technology to find solutions. This issue is covered in Section 3.5 exploring individual skills and interpersonal capabilities.

Business benefits of diversity may arise from, for example, improved decision-making as a result of being able to respond more easily to complex challenges, and in providing more challenging thinking.[52] The presence, for example, of increased thought or experience diversity (in other words, the opposite of 'groupthink') is seen to be a crucial part of creating a more effective board. Directors with different experiences, knowledge and perspectives on society lead to greater responsiveness in decision-making.[53]

For example, a governance academic from South Africa said that diversity:

> *"…strengthen[s] your board because it will give you diversity of outlook. I mean it's the right thing to do in any case, but it has to be attached to performance, and the whole point of diversity is to strengthen the decision making." (7)*

3.2.1.5. Challenges to increasing board diversity

This section on 'challenges' reflects the dynamics which may work against the trend, or which provide nuance to the trend, rather than being an evaluation of whether or not the trend itself is desirable.

The overall take-away from our interviews was that there appears to be little systematic focus on how to create a truly diverse board – an issue that is explored further in Section 3.4 on Board dynamics. We are also in the very early days of moving beyond defined characteristics (such as gender and ethnicity).

> *"The boards I've served on have been very interested in optics and so they have not done a deep dive into what diversity really means, what inclusion really means, what equity means." (19)*

An additional problem with solely concentrating on a demographic approach to promoting diversity, is, as referred to by several interviewees, that of limited ideas of what diversity could and should be. This narrow focus therefore misses the benefits of, for example, cognitive diversity and diversity of experience, which is only just emerging as an area of attention, as noted by a recruitment consultant from an executive search firm:

> *"What's evolving now in addition to ethnic diversity is diversity of perspective. Right. So yeah, which is very good. So just because someone is ethnically diverse, if they went to the same school and group in the same neighbourhood as the CEO, is that really a different perspective? … The perspective diversity is a new thing for sure." (29)*

A number of interviewees also mentioned the danger of boards just engaging in diversity to tick the appropriate box, in other words, treating diversity as a compliance issue. Examples were given of boards looking for individual candidates who were able to tick multiple boxes, such as gender, ethnicity, sexuality and technical background simultaneously in order to meet diversity requirements.

3.2.1.6. Likely trend trajectory of board diversity

We expect these trends towards increasing board diversity to continue worldwide as a result of both the changing legislative and regulatory context, as well as the perceived and actual positive impact of diversity in a business context, including dealing with complex challenges such as sustainability (see Section 3.6 on Board membership, structure, dynamics and skills: concluding reflections, as well as related pressure from stakeholders, including shareholders.

3.2.2. Trend 2: Increasing numbers of strictly independent NEDs

There is a trend towards gradually increasing numbers of strictly independent non-executive directors (NEDs) as a proportion of the board.

'Strictly independent' NEDs are defined here through their fulfilment of a set of rigorous criteria, identified by the Refinitiv Eikon Global Database. These identifiers include having no direct personal or financial links with the company, and not owning more than 5 per cent of the company's shares.

A number of interviewees referenced the importance of independent and non-executive directors in relation to board composition and diversity.

> *"I see a lot of discussions in relation to the board composition, especially non-executive directors and independent directors – how many, and how hard it is to have a balanced board." (23)*

Some interviewees felt that the number of general non-executive, and particularly 'strictly independent' NEDs, is increasing. However, the Refinitiv Eikon data only identifies an overall increase in the number of 'strictly independent' directors, and not in NEDs per se, which is in fact static.

Refinitiv Eikon defines 'strictly independent' directors as: not being employed by the company; not having served for more than ten years; are not +5 per cent reference shareholders (in other words, they must not own more than 5 per cent of the company's shares, and related voting rights); have no cross-board membership; no recent family ties; and no company compensation beyond board services.

Table 13: Percentage of non-executive directors (NEDs) on boards (2017–21)

	2017	2018	2019	2020	2021	2022
% of NEDs	76.0	76.7	76.8	77.4	77.8	(74.6)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

The Refinitiv Eikon data shows that the number of NEDs per se on boards, while high at over three-quarters, was static between 2017 and 2021.

There is geographical variation with the lowest percentage being 69 per cent in Asia, and the highest at 84 per cent in Europe. For sectors, there is no discernible trend.

We explore the culture of board independence more fully in Section 3.4 on Board dynamics. Here we only look at the numerical trend relating to the numbers of strictly independent directors on boards.

Table 14: Percentage of strictly independent non-executive directors (NEDs) (2017–21)

	2017	2018	2019	2020	2021	2022
% of NEDs	76.0	76.7	76.8	77.4	77.8	(74.6)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

The data shows that globally the numbers of strictly independent NEDs on boards is slowly climbing, accounting for around half of board membership worldwide.

There is geographical variation with a low of 36.7 per cent in Asia in 2021, and a high of 57.8 per cent in Northern America. Within sectors, the lowest percentage of 45.5 per cent is found in 'Consumer staples', and the highest in 'Health care' at 57.8 per cent.

In some geographical contexts, especially those characterised by a high concentration of family ownership, the number of independent directors is much lower. For example, Spencer Stuart recently reported that in Turkey only 35 per cent of directors meet the local criteria for independence, and in Chile the figure sits at 20 per cent.[54]

3.2.2.1. Drivers to increasing numbers of strictly independent NEDs

The drivers that have led to the high percentage of NEDs, as well as increasing numbers of strictly independent NEDs, have mostly arisen from the impact of corporate governance and stewardship codes as outlined in **Phase 1: Part 2**, as well as good board practice.[55]

There is an additional rationale for this high level arising from the business case driver to increase 'board capital' – the ability of NEDs to offer boards more diverse resources based on their external experiences, networks and life expertise, as well as specific functional skills.[56] The active choice of diversity in NEDs is therefore one of the key ways to achieve diversity on boards.

Research by Petra (2005) suggests that the presence of NEDs strengthens boards – bringing pluralism, experiences beyond the sector, different backgrounds, personalities and cultures, as well as gender and other diversity.[57] Banerjee et al. (2020)[58] and Garner et al. (2017)[59] both review a range of academic literature that suggests that NEDs are presumed to be better able to scrutinise management and counter any tendency towards short-termism from either management or shareholders, hence supporting long-term value creation, a view also reiterated by EY (2018) in their overview of the independent board leadership landscape.[60]

As part of an effective board, Morten Huse has argued that NEDs are expected to embrace tension and dissonance between the following factors:[61]

- distant and close
- independent and interdependent
- trusting and distrusting
- engaged but non-executive
- challenging and supportive
- informing and questioning
- dissenting and respectful.

He believes that it is easier for independent NEDs to navigate these tensions more than executive directors or other 'inside' actors. As such, truly independent NEDs may be able to question better board strategy and hold the board more generally to account.

3.2.2.2. Challenges to increasing numbers of strictly independent NEDs

Getting the right balance of truly independent and senior executive managers is difficult. Independent NEDs are only one way to create a diverse and independent board, capable of making considered decisions without undue influence from influential stakeholders or their own best interest. This challenge is further discussed in Section 3.4.1.1 on the culture of board independence.

Several interviewees pointed out that another significant difficulty is the limited pool from which to recruit appropriate NEDs.

> *"All boards are taking meaningful steps to increase diversity, but it will take some years for a deep pool of diverse NED talent to emerge. Finding ways to support and develop this is important." (8)*

3.2.2.3. Likely trend trajectory of strictly independent NEDs

The number of strictly independent NEDs on boards is likely to climb and then stabilise in the coming years. This trajectory is suggested because there is likely to be an upper limit to the desirable number of NEDs (although this level is unclear). Trends in certain countries would therefore slow down and perhaps stop. Because different geographies are moving from different baselines, there will therefore be an element of 'catch up' in some places which have further to go, and which will hence show further increases.

3.2.3. Insights into board size and tenure

Two issues relate to the capacity of the board to adequately and appropriately fulfil its roles, including realising its diversity, and relative independence. These are board size and tenure. We use data from the Refinitiv Eikon database to assess what is happening empirically.

3.2.3.1. Insight into changes in the size of the board

Perception of the optimum board size is likely to vary according to stage of development of the company, number of board committees required, and the balance of skills and experience required. Much of the recent focus on board size comes from changes in regulatory concerns (for example, those specifying minimum requirements) and the increased importance of independence and diversity.[62]

The Refinitiv Eikon data can provide granular data on the number of people who sit on boards (globally, geographically and by sector).

The number of people sitting on boards internationally is static at around nine, although varying from six to 11 geographically.

Table 15: Average board size around the world (2017–21)

	2017	2018	2019	2020	2021	2022
Board size	9.5	9.4	9.2	8.9	8.9	(8.6)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

The data for board size shows a small decrease from an average of 9.46 in 2017 to 8.94 in 2021. However, there are differences between countries with a range in 2021 from around six to 11. The highest average is in Africa at 11.0, and the lowest in Oceania at 6.3. Most countries show relative stability over time. The slight decrease in board size is predominantly accounted for by the number in the UK falling from 8.5 in 2017 to 7.4 in 2021, and in Europe from 9.7 to 7.9.

Across sectors there is a relatively more even spread between just over eight, and approaching ten.

The 2022 UK Spencer Stuart Board Index, which looks at the largest 150 companies in the FTSE rankings by market value at 30 April 2022, reports that the average board size is ten. This figure has been consistent for the past decade. Thirty-eight per cent (57) of boards comprise more than ten members, the largest boards being WPP and Berkeley Group Holdings with 15 members each.[63]

3.2.3.2. Insight into length of time board members sit on a board (board tenure)

Board tenure shows relative stability at around seven years, but with some geographical variability.

Table 16: Average board tenure globally in years (2017–21)

	2017	2018	2019	2020	2021	2022
Board tenure (years)	7.40	7.25	7.14	6.94	6.94	(7.16)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

The length of time for which people sit on boards has shown a slight decrease, but is roughly level at about seven years globally. There are geographical variations in the latest year for available data (2021), with a low of 4.59 in the UK and a high of 6.44 in Africa. There seems to be little sectoral variation.

With regard to board tenure, Papadopoulos (2018) acknowledges that some investors consider excessive director tenure as a factor that could compromise independence.[64]

Morten Huse stated that the argument for setting limits on board tenure is important since a shorter period of time increases the ability to challenge executive management without becoming too habituated to what is assumed possible.[65]

Other research such as that by Elms and Pugliese (2022), however, indicates that these observed correlations are not straightforward,[66] and Papadopoulos (2018) concludes that long tenures do not necessarily mean a diminishment of contribution or performance.[67]

> *"The stats are there, aren't they? That tenure of directors is shorter and shorter and have been getting shorter for some time and that does give you a challenge because you have a strategy reset necessarily when leadership teams change. And then you can lose time and people are starting again and learning again. So that could be an issue as well." (6)*

3.3. Board structures

We now turn to our second thematic area: board structure. A number of our expert interviewees made the overall point that, because of the increasing responsibilities being placed on board members, and the fast-paced and changing nature of the issues that need to be discussed, there is growing attention being paid to how best to structure the board and its sub-committees.

There seems to be little agreement, however, on how best to do this restructuring, particularly given the lack of evidence of the superiority of one approach over another. Companies seem to be feeling their way towards good practice, with a recognition that there is:

> *"…no one-size-fits-all answer. There are different ways of doing this. Some may or may not be more effective than others." (7)*

This latter respondent, a governance academic, added that, as a result of this challenge, it was a topic which he was:

> *"…talking to a lot of boards about. Who should be in the different committees? … Who should have what, and what does good look like?" (7)*

The scope of these considerations includes the division of responsibility between the main board and sub-committees, the size of the board (Section 3.2.3), as well as the relationships of all these aspects with the wider governance architecture, such as external advisory councils, shadow boards etc (see Section 4.6.4 for examples of innovation in this space).[68] There seemed to be a particular lack of agreement about whether or not there should be a separate ESG or sustainability committee, or whether these functions should rather be carried out by the main board. We explore these implications further in Section 3.6 on Board membership, structure, dynamics and skills: concluding reflections.

3.3.1. Trend 3: Increasing discussion of appropriate board structures, with an increase in sustainability-related sub-committees

As a result of both legislation and voluntary corporate codes around the world, many boards of large companies are already required to have various standard sub-committees such as risk committees, audit committees, corporate governance committees, and nomination committees (see **Phase 1: Part 2**). Sub-committees are presumed to offer boards three main benefits: knowledge specialisation, division of duties, and accountability.[69]

An overall trend emerged from the views of the expert interviewees.

There seems to be a growing debate about how to structure boards and sub-committees, with a trend towards increasing numbers of sustainability-related sub-committees, albeit with some concern expressed over their effectiveness.

The Refinitiv Eikon data is able to provide more granular data to identify sub-trends (globally, geographically and by sector) on a variety of related issues. These cover:

- sustainability-related sub-committees
- nomination sub-committees
- audit sub-committees.

3.3.1.1. Board structures sub-trend: sustainability-related sub-committees

Sustainability-related sub-committees appear to be on a rapid rise among listed companies, although with different levels geographically and across sectors.

Table 17: Percentage of 'CSR sustainability' sub-committees on boards (2017–21)

	2017	2018	2019	2020	2021	2022
% of CSR sustainability committees	40.1	41.5	45.5	49.6	57**	(71**)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers **Percentage data here could only be accessed at whole number level

The Refinitiv Eikon data indicates that the number and rate of growth of what they call 'CSR sustainability' committees in the world's largest companies rose from 40 per cent to 57 per cent between 2017 and 2021. The criteria used to determine this data are that these companies "have a CSR committee or team", or a "board level or senior management committee responsible for decision making on CSR strategy" with CSR here taking on a more inclusive definition to include sustainability, and ESG concerns. As a result, we can use this data as a tentative proxy for what could be more broadly called sustainability-related sub-committees. An additional and important point to note is that this data on 'CSR sustainability' sub-committees, however, may not specifically indicate actual board sub-committees, or be only about the board.

The Sustainability Board Annual Report assesses the level of ESG engagement by the boards of directors of the world's 100 largest public companies.[70] One proxy used for this assessment is the prevalence or otherwise of sustainability or ESG-related sub-committees for the top 100 of the world's largest publicly listed companies, drawn from publicly available website data. In 2019, on this basis, 54 per cent of boards had a relevant ESG committee, with geographical variation between the highest, the US, at 71 per cent, and the lowest, China, at 22 per cent, and in Japan, 25 per cent. In 2020, this figure rose to an aggregate level of 71 per cent, with similar geographical variation. It remained static in 2021, and rose to 80 per cent in 2022. It is important to note that the measure changed between 2020 and 2021 to include both sub-committees and/or a dedicated sustainability/ESG policy for a relevant sub-committee.

The latest findings from the 27th annual Spencer Stuart 2022 study into the top UK FTSE 150 companies found that 30 per cent (46) of the firms researched had board committees to oversee sustainability issues, such as decarbonisation, human rights, climate change and good citizenship.[71] This was a nearly 50 per

cent rise from the previous year, reinforcing the possibility that there has been a significant upturn in the last year or so.

For the richest companies, a study by EY found that 85 per cent of Fortune 100 companies had a board committee which oversaw ESG matters – up from 78 per cent.[72] EY's paper also notes that sustainability-related matters are spreading among various sub-committees.

This wider coverage was also found in a PwC report showing that ESG matters are increasingly issues for all directors, whether or not there is a specific board sub-committee.[73] Fifty-two per cent of directors surveyed said ESG issues were now regularly part of the main board agenda, up from 45 per cent in 2020 and 34 per cent in 2019.

Table 18: Geographical percentages of 'CSR sustainability' sub-committees on boards (2021)

	Africa	Asia	Europe	Latin America and the Caribbean	Northern America	Oceania
% of CSR sustainability committees	66	53	58	73	37	47

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); Percentage data here could only be accessed at whole number level

Looking at geographical differences, the Refinitiv Eikon data in Table 18 shows the lowest levels in Northern America (37 per cent in 2021) with the highest in Latin America and the Caribbean (at 73 per cent). In terms of sectors, the lowest activity is in 'Health care' (23 per cent), and the highest in 'Utilities' (68 per cent).

The international recruiter firm Russell Reynolds Associates believes that geographical differences depend on the company's specific context, board culture, industry, and regional norms. In their survey of listed companies only 13 per cent of S&P 500 (listed on US stock exchanges) companies have a dedicated committee tackling ESG matters, versus 33 per cent of the DAX (German), and 54 per cent of the FTSE 100 (UK).[74]

However, care needs to be taken with much of this data, whether from Refinitiv Eikon or consultancies. In one of the workshops for this research, the suggestion was made that the trend may significantly vary for publicly listed and privately owned companies – a dynamic that will be explored further in Phase 2 of the research.

3.3.1.2. Board structures sub-trend: nomination sub-committees

Nomination sub-committees are increasing globally at a slow rate, but from a high base, and with significant variation in levels geographically.

Table 19: Percentage of nomination sub-committees (2017–21)

	2017	2018	2019	2020	2021	2022
% of nomination committees	77.1	76.7	75.9	74.8	79.6	(86.0)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

The prevalence of the nomination sub-committee is at a fairly high and steady level, and is found in more than four out of five boards.

However, there is variation between countries, with a high of 90 per cent in Northern America, and only 25 per cent in Latin America, but with little variation across sectors.

The nomination committee has historically focused on the succession planning of directors, or of the CEO. There has also, however, been discussion about its wider role in assessing and ensuring that the board is performing well, for example through considering the level and type of board member skills needed.[75]

Deloitte's proxy research with S&P 500 companies on emerging trends in ESG governance for 2023 suggests that the nomination and corporate governance committees remain the most common choice for sole or primary oversight of ESG at 63 per cent of reporting companies, up from 53 per cent last year, with 15 per cent of companies placing primary responsibility for ESG on a dedicated ESG/sustainability committee, similar to the 13 per cent in 2021. The report also noted, however, a significant shift towards a multi-committee approach, given the significant enhancements in the depth and detail around ESG proxy disclosures and related governance frameworks. Fifty-one per cent of companies reported that either (i) the full board combined with a committee(s) or (ii) multiple committees have responsibility for overseeing aspects of ESG activities.[76]

One large recruiter has claimed that the core functions of the nomination committee have never been more needed. It is highly scrutinised by investors, who will vote against a board if they think it is falling short in its composition and capability qualities, such as in its gender and ethnicity mix, or in its ability to meet its ESG commitments.[77] This latter view is supported by KPMG, which argued in a recent briefing paper that the oversight of a quality ESG-savvy board begins and rests with a competent ESG-skilled nomination committee.[78]

3.3.1.3. Board structures sub-trend: audit committees

Audit committees are at a high and steady level globally, except in Latin America where the level is significantly lower.

Table 20: Percentage of audit sub-committees (2017–21)

	2017	2018	2019	2020	2021	2022
% of audit committees	92	92	91	89	92	(92)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

Geographically most regions cluster around the high level of around 92 per cent in 2021, with the exception of Latin America at 70 per cent. All sectors show similar percentages.

In 2022, a report by The Center for Audit Quality based on 49 interviews with audit committee (AC) chairs in the US (30 respondents) and other related professionals (19 respondents) concluded that perpetually assigning emerging risks to the AC (ie the 'kitchen sink' approach) can lead to suboptimal oversight due to overworked ACs and a 'check the box' mentality. The report recommends that AC skill sets evolve from traditional financial reporting and internal controls – purposefully developing skill sets that match oversight responsibilities.[79]

3.3.1.4. Drivers of trends in board structure

The main drivers of trends in board structure are likely to relate to the corporate governance and investor governance frameworks covered in Phase 1: Part 2. The trend towards sustainability-related sub-committees is thought likely to have arisen from the increasing legal or investor requirements to report on company ESG measures, as well as stakeholder (including investor) pressure to act. These factors probably explain their preponderance in listed companies, but may not be as significant a driver for those that are privately owned (an issue that will need to be further explored).

3.3.1.5. Challenges to trends in board structure

Some of our interviewees queried the effectiveness of sustainability sub-committees. For example:

> *"Ten years ago you … wouldn't have found a sustainability sub-committee. I think in most companies you do now … I think there are more … that most boards have got such a thing … but I think it's too early, certainly, from my perspective … to say whether this is working, whether it's producing good results or not." (7)*

There has also been some concern that sustainability sub-committees could marginalise sustainability issues. It was suggested that this could be a place where the 'diverse' candidates are put, in some ways implicitly signalling a reduced or marginal importance of that function.

3.3.1.6. Likely trend trajectory of board structure

The rise of sustainability sub-committees is likely to continue to grow as ESG and sustainability issues become more important to investors, and to wider stakeholders.

Although our data shows a relatively static trend in the percentage of nomination committees over the past five years (the 86 per cent figure for 2022 is only indicative) – the increasing importance surrounding the nomination function suggests it is likely to increase, or at least be maintained, as a way to ensure a diverse board, capable of addressing current and future challenges. While remaining fairly static in number, there are also changing skills and responsibilities required of audit committees. The impact of the nomination committee will depend on effective interaction (relating to the division of function and the terms of reference) within the board, and its empowerment from the main board to realise its aims, otherwise it may continue to be nominal rather than effective.

3.4. Board dynamics

We turn now to our third thematic area of relevance to this domain: board dynamics. The way in which board members inter-relate, discuss and debate among themselves – dynamics that are strongly shaped by board culture and power differences – fundamentally determines the effectiveness or otherwise of a board's ability to make strategic decisions and conduct appropriate oversight.

Board dynamics is a particularly difficult area to investigate, and as a result is under-researched. Our expert interviewees, however, raised many and various insights into this area in nearly all interviews. While it is too soon to identify definitive trends in what is actually taking place in boardroom cultures across the globe, this early analysis suggests that this area would benefit from further systematic analysis, as well as practical support and guidance for boards.

3.4.1. Trend 4: Increasing attention being paid to board dynamics and board evaluations

Board dynamics was one of the most significant themes emerging in the Global Trends Survey. The insights from expert interviewees, as well as some supporting data from the Refinitiv Eikon database, enable us to suggest a broad trend in this area.

There is growing awareness of the importance of board dynamics, which is also reflected in what appears to be increasing numbers of board evaluations. There are indications that some boards are slowly evolving to become more inclusive and independent from both executive management and controlling shareholders, although this trend appears to be culturally and geographically variable.

The importance of understanding board culture is underscored by the number of professional firms – consultants, recruiters and educationalists – that study or support this area. For example, Spencer Stuart argues that a healthy culture is critical to good board performance.[80]

A 2022 report by PwC warned that four potential behavioural biases could undermine board culture and dynamics:

- authority bias (reflecting expertise and/or power dynamics)
- groupthink (over-prioritising harmony and conformity)

- status quo (sticking to how it is now) bias (and relatedly sunk-cost bias, leading to an aversion to change)
- confirmation bias (subconsciously seeking evidence that supports our own beliefs).[81]

A range of factors have been suggested as likely to influence the overall culture of a board, and how people inter-relate.[82] These include:

- the diversity of board members (see also Section 3.2.1) and whether and how this potential is realised to support good decision-making
- the independence of the board, specifically a dynamic of independence from executive management, and other influences such as controlling shareholders (Section 3.4.1.1)
- the skills of the chair (Section 3.4.1.5.3)
- board members' interpersonal skills (Section 3.5).

In addition, and particularly relevant when considering board dynamics worldwide, cultural differences, including differences in national cultures, can affect levels of interpersonal trust, or the ability to challenge or be frank in one's opinions.[83] Some cultures may support more collaborative dynamics, whereas others may have pronounced inequalities in distributions of power and voice, or be more naturally hierarchical and conformist.

Awareness of power dynamics is a particular issue in relation to diversity. These power differences can potentially undermine efforts to bring different voices and experiences into the boardroom.[84] There seems, however, to be little research into how to change board practice to counter these difficulties within different contexts.[85] These considerations are likely to be particularly important in cultures where power differences, or concentrations of family ownership, are high.[86]

Among board director training providers, a growing number of educationalists are addressing issues such as power and culture in their board programmes, in response to client need.[87]

Five main insights, which overlap with the structural shifts noted in the previous sections, arose from our expert interviewees. These were:

- the importance of independence in terms of board behaviour, rather than just the numbers of NEDs (Section 3.4.1.1)
- indications of a shift away from hierarchical decision-making towards a more collegiate approach (Section 3.4.1.5.1)
- growing appreciation of the importance of group dynamics and culture for realising the potential of board diversity (Section 3.4.1.5.2)
- a particular emphasis on the importance of how the chair manages boardroom dynamics (Section 3.4.1.5.3)
- importance of board evaluations as one way to determine whether board dynamics are positive or negative. Board evaluations appear to be increasing around the world, albeit with variable quality (Section 3.4.1.5.4).

3.4.1.1. A rising culture of board independence

In addition to the numerical data on strictly independent NEDs that we explored in Section 3.2.2, the Refinitiv Eikon data also allows us to look at more granular sub-trends that can have a bearing on a culture of independence within board dynamics:

- there is a slowly rising number of companies having a written policy and/or practical interest in ensuring the independence of their boards
- the roles of chair and CEO are increasingly separate
- there is a slight decrease in the number of CEOs on boards (although this result is difficult to interpret since the data mix unitary boards where it is the norm, and supervisory boards where it is not).

3.4.1.2. Board independence sub-trend: policies on board independence

There is a slowly rising number of companies having a written policy and/or practical intention concerning the independence of their boards.

While we have already looked at the relative composition of the board in terms of NEDs, and specifically strictly independent NEDs, this does not necessarily mean that the board dynamic itself is truly independent. One indication of intent, although not of necessary impact, is whether or not boards have a stated policy to work in an independent way. This is only a weak signal, since this kind of policy is generally required by different corporate governance codes, and does not indicate the extent to which independence is actually operationalised. We explore the implications of board independence for sustainability outcomes further in Section 3.6 on Board membership, structure dynamics and skills: concluding reflections.

Table 21: Percentage of boards with a policy on independence (2017–21)

	2017	2018	2019	2020	2021	2022
% of boards with an independence policy	67.9	68.7	70.9	71.9	74.2	(67)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

We found, using the Refinitiv Eikon data, that around three-quarters of global companies now have a policy asserting board independence, up from 68 per cent in 2017. (The lower number in 2022 may be an anomaly.)

The percentages quoted here are calculated using the following criteria:

- whether or not the company has a policy regarding the independence of its board
- the company strives to maintain a well-balanced board through an adequate number of independent board members
- independent board members maintain integrity and independence in decision-making.

Across geographies the lowest percentage is in the UK (50 per cent) and the highest in Northern America at 90 per cent. There was some variation among sectors globally, with the lowest percentage of 71 in 'Communication services' and the highest at 82 per cent in 'IT' and 'Health care'.

Another aspect of independence relates to whether or not the chair of the board and the CEO are the same person.

3.4.1.3. Board independence sub-trend: CEO/chair separation

The roles of chair and CEO are increasingly separate.

The Refinitiv Eikon data indicates that there is a global increase in the trend for the two senior company roles of board chair and operational CEO to become increasingly separated, in other words, not performed by the same individual.

Table 22: Percentage of boards with combined CEO and chair roles (2017–21)

	2017	2018	2019	2020	2021	2022
% of boards with CEO/chair combined (or chair was CEO)	35.0	33.9	32.9	31.2	29.5	(27)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

The country with the highest level of separation, in other words the lowest level of combined CEO/chair, is the UK at 11 per cent, and the region with the highest number of combined CEO/chairs is Northern America at 43 per cent. There is variation across sectors, with 20 per cent in 'Utilities' and 27 per cent in 'IT'.

A 2020 article by Joseph Mandato and William Devine in the *Harvard Business Review* (HBR) in the USA, where the combining of the roles in one person has been a long-held and common practice, called for a rethink. Following substantial corporate failings at Boeing (737 MAX system flaws), WeWork (billion dollar losses following over-expansion) and Facebook (Russian interference in US elections), the authors argued that if the same person occupies both roles, the right questions may not be asked; and deep independent scrutiny could be compromised.[88]

There has also been a parallel rise in the number of independent chairs, particularly in the UK, Europe and the USA. For example, research from the EY Center for Board Matters reports a shift towards independent board chairs among S&P 1500 firms from 27 per cent in 2000 to 60 per cent in 2018, mirroring a significant increase in independent directors from 65 per cent in 2000 to 83 per cent in 2018.[89]

3.4.1.4. Board independence sub-trend: the presence of the chief executive on boards is decreasing slightly

The Refinitiv Eikon data shows that the number of chief executives who take a seat on their company's main board is falling slightly overall (however, the increase in 2022 may or may not be an anomaly and will need to be checked when full figures are available).

Table 23: Percentage of boards including the CEO (2017–21)

	2017	2018	2019	2020	2021	2022
% of boards including the CEO	87.3	84.7	84.1	83.4	82.2	(89.1)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

The presence of the CEO on boards is decreasing slightly.

There is considerable variation by region, with the lowest percentage at 49 per cent in Europe and the highest at 97 per cent in Northern America and the UK. Regional trends have all shown slight drops, except in Northern America and the UK which have remained at the same high level.

The lower percentage in Europe merits further investigation and may be due to different governance structures, such as the German model of having a supervisory board which appoints, supervises and advises the management board.[90] It is not necessary that a CEO sits on a unitary board (although, as the data indicates, for unitary boards such as those in Northern America and the UK, this is normally the situation. Further research may be necessary to find out if it is required in some jurisdictions). The current data suggests that the presence of the CEO on the governing board is the dominant norm.

Sectors show less variability, with 74 per cent in 'Consumer staples' at the lowest, and 91 per cent in 'Health care'.

3.4.1.5. Changing interpersonal dynamics

The expert interviewees suggested that there are several observable changes happening in interpersonal dynamics:

- a shift from hierarchy to more collegiality (Section 3.4.1.5.1)
- the recognition of the importance of group dynamics and culture for realising the potential of board diversity (Section 3.4.1.5.2)
- the skills of the chair (Section 3.4.1.5.3)
- a rise in board evaluations, and with a focus on board dynamics (Section 3.4.1.5.4).

3.4.1.5.1. Interpersonal dynamics insight: a shift from hierarchy to collegiality

The comments from interviewees suggest that there has been an evolution away from a one-way control of information provided by the CEO or executive, and with responses to that information controlled by the chair, to greater discussion and deliberation between board members.

This insight is potentially being supported by recognition of the need to build a more collegiate and deliberative dynamic, rather than one which just focuses on individual opinions and voices.

> *"I'm seeing a shift … I think that's evolved and you have much more really good discussions around the boardroom table." (11)*

"there's more attention paid to … team building with the board … I think that's really important to work effectively … I've seen a little bit more space for discussion, not always, but the boards that work more effectively, there's more discussion time…" (20)

"I think what they look for are people who will be very participatory, right? So they're not going to sit there and rubber stamp everything. They're going to be very actively contributing to conversation, to debate, challenging other board members, challenging management." (29)

3.4.1.5.2. Interpersonal dynamics insight: the recognition of the importance of group dynamics and culture for realising the potential of board diversity

A number of expert interviewees referred to the importance of board dynamics and culture in the context of board diversity. One recruitment consultant for a US executive search firm – while reflecting on recruiting for diversity – commented that:

"So we are asked by our clients to filter the applicant pool of potential board director appointments by not only their technical expertise and executive acumen, but also culture fit with the board … we need to make sure that we are delivering candidates who are not only a fit experientially, but who are a cultural fit, both with the current culture of the board and also perhaps the aspirational culture of the board." (29)

Other interviewees reflected on how, when there is an absence of a focus on culture and group dynamics, this can impede the realisation of the benefits of diversity:

"The dynamics in some boardrooms could be improved … Who do we have around the boardroom table, and why do we have these people?" (11)

Concern was expressed that, despite the previously identified trends towards greater diversity, these will not make any difference unless there is a fundamental shift in how these views are incorporated into decision-making.

"I think I physically see diversity, but I don't see diversity in the board dynamics." (26)

PwC's 2019 Annual Corporate Directors Survey, based on 734 public company directors in the United States, reported that 43 per cent of directors say it is difficult to voice a dissenting view in the boardroom.[91]

3.4.1.5.3. Interpersonal dynamics insight: the skills of the chair

A number of expert interviewees felt that the chair was crucial to creating a positive board dynamic, and making the most of the board's skills and diversity.

"By definition, the more diverse you are, the dynamics change. It's less about a kind of natural consensus of like-minded people … this is the chair's role to ensure this works effectively." (28)

The Miles Group and Rock Center for Corporate Governance at Stanford University survey found that only 72 per cent of 187 US directors believed that their chair was effective in encouraging the participation of all directors, with only 68 per cent believing they were effective in inviting the participation of new members.[92]

An interesting point, raised by a leadership consultant from the Americas, was that the diversity of the chairs themselves could also be an important factor in board dynamics.

> *"If the board chair is a person who comes from a non-dominant culture … then that agenda is going to look a little different [because] … well-being … is so important for most non-dominant culture people … they know what it's like not to be cared for in a system." (19)*

Korn Ferry's European Board Practice undertook a study in 2020 to determine the qualities that will define board chairs in the 2020s. Ten qualities were identified: (i) breadth of experience, with boards and beyond; (ii) intense curiosity and openness to difference; (iii) resilience, self-mastery and strength of character; (iv) emotional intelligence and exceptional communication skills; (v) humility and (a personal) growth mindset; (vi) intellectual acumen and ongoing mental agility; (vii) collaboration mentality, and an appreciation of partnerships; (viii) a sense of purpose; (ix) digital awareness and capability; and (x) total commitment to and engagement with the role.[93]

The Deloitte Global Boardroom Program interviewed and surveyed more than 300 chairs from 16 countries (Australia, Belgium, Canada, China, East Africa (Kenya and Uganda), Germany, India, Ireland, Italy, Japan, New Zealand, the Netherlands, South Africa, the United Kingdom and the United States) to get a better sense of how the position is changing and what the chair of the future can expect. The findings suggested convergence around five fundamental areas of change (organisational governance needing more chair input; society expecting more of business; climate change requiring business to respond; crisis leadership becoming the norm; and boards now operating in hybrid and agile modes) and identified eight leading practices for being a board chair:[94]

1) Build relationships. Create bonds with the board, management, stakeholders, and, especially, with the CEO, while also maintaining detachment and independence of thought.
2) Show decisive leadership. Empathy is important, but so is being assertive, when necessary.
3) Understand the business. Chairs will struggle if they do not know the many facets of the business, its operations, people, competitive landscape, and culture.
4) Lead on purpose and values. Chairs must make tough and, at times, unpopular decisions in the long-term interest of the reputation of their organisations.
5) Be a learning leader. Confronted with many unknowns, chairs must be comfortable asking for help and continuing to learn and lead a 'learning board'.
6) Nurture a broader skill set. Technical skills matter, but so do emotional intelligence and the ability to draw out the best in others.
7) Embrace diversity. Diversity in all its forms drives productive debate and discussion and helps prevent groupthink.
8) Be a good listener. Adding value to the organisation requires listening to those around you, especially when opinions vary, to ensure views are fully explored before drawing a consensus.

3.4.1.5.4. Interpersonal dynamics insight: evaluating the board

There are indications that board evaluations are slowly increasing around the world at different rates, although their quality is variable.

Board assessments are one way to investigate whether or not the dynamics of a board are positively supporting effective decision-making and oversight (in relation to the particular goals of the company, which will vary depending on its logic: CSR, ESV, or Purpose driven). From the comments made by some interviewees, boards seem to be increasingly looking not just at processes and procedures, but also at the people themselves, who they are, and why they sit around the table. In fact, about a fifth of interviewees thought that board evaluations were increasing, and gaining greater prominence.

A governance consultant based in the UK said:

> *"In certain regions [board evaluation is] taken very, very seriously … That is evaluating the board … board committees … individual directors … the board secretary or the company secretary. It's evaluating the chair … the CEO and the executive management team … It's doing everything." (22)*

The interviewee further reflected that:

> *"And if that's been done rigorously, at least every three years by an external professional, then that is a huge tool associated with improvement and change and dynamics … It's an incredible tool for improving the efficacy and the effectiveness of the board." (22)*

A survey of 236 public companies on board evaluation practices by Korn Ferry in 2021[95] identified culture and dynamics as one of three top focus areas for boards.

The Russell Reynolds Associates 2022 Global and Regional Trends in Corporate Governance saw board evaluation as a governance trend to watch in 2022.[96]

Some of the expert interviewees expressed concerns, however, that while board evaluations can be very useful, many are not rigorous or independent enough.

> *"A considerable proportion of board evaluations [are] not very rigorous … They're not firstly independent. There's connections, with particularly the chairman at some historic point in the past … They've now retired and they're able to devote some time to evaluating a board … They're not necessarily best practice … and they're not being rigorous enough in terms of their comments and their criticisms." (22)*

In 2019, the Center for Creative Leadership conducted 350 interviews with board members across six countries in Asia. This revealed that culture and group dynamics are perceived by respondents to be critical for board effectiveness, yet board evaluation processes are often deemed to be inadequate.[97]

PwC's 2019 Annual Corporate Directors Survey, based on 734 public company directors in the United States, found that more directors say their boards are taking action on board performance assessments (72 per cent, up from 49 per cent in 2016) but most focus on adding expertise or diversity, rather than the more difficult tasks of counselling or not renominating directors.[98]

3.4.1.6. Drivers of board dynamics

One of the key drivers for the growing awareness and scrutiny of board dynamics has been a series of high-profile governance failures, which have drawn attention to why seemingly robust governance arrangements have failed to perform.[99]

There has also been much more appreciation of the value of having an independently minded and behaving board. Investors and other stakeholders are realising that good independent composition, continual refreshment of the board (see Section 3.2.3 on Board tenure), and good board evaluation practices (Section 3.4.1) can result in improved corporate performance and decreased risk exposure.[100]

Morten Huse argues that the idea of independence goes beyond a focus on NEDs. The goal is to build an entire board of directors which balances these tensions of "involvement and distance … dependence versus independence".[101]

If general independence is not supported or enabled, then a 'passive' dynamic might be established. This could also happen if board directors continue to be re-elected by equally passive shareholders. The result can be unequal power dynamics within the board, particularly with executive management, and overall poorly functioning boards.[102] This danger is recognised not only in governance codes but also in proxy voting guidelines in the UK and US. The latter explicitly advise investors to question issues around independence. For example, Institutional Shareholder Services (ISS) in its UK proxy voting guidelines, has recommendations to vote on board independence.[103]

These issues are complex, as cultural dimensions are likely to strongly influence group norms and dynamics. As one interview noted, with reference to a particular jurisdiction in Asia and the reaction of some shareholders:

> *"You know, they're kind of shocked by how passive some board members are. You know, they just sort of just nod and agree with company management." (Workshop P1)*

As identified in **Phase 1: Part 2**, the related rise in litigation is likely to have created a less passive dynamic by board members in relation to each other, and to the executive, in terms of being more aware of others' behaviours and views which may invite litigation, as well as potentially increasing risk aversion which could act as a barrier to innovation and more disruptive change.

In 2021, the Intersearch Global Board Survey reported that 69 per cent of the 1,782 respondents from 79 different countries and legal jurisdictions believe their potential liability risk has increased over the past 24 months, with 19 per cent considering their Directors and Officers Liability Insurance to provide insufficient cover.[104]

One interviewee, who sat on a non-profit board, also made the point that generational shifts were important in driving changing dynamics:

> *"It's just my experience, with some of the younger board members, the students, there's a real demand for democracy and representation … whereas I would say with some of the older generation who I work on boards with, it's much more of a command and control style, or we're here to talk to the executive team. It's not quite so representative and inclusive." (20)*

The 27th edition of the long-standing board survey of the UK's top 150 FTSE companies, by global headhunter Spencer Stuart, showed in 2022 a desire for 'fresh' NEDs.[105]

The perceived value shift within boards could well reflect the complex and volatile external environment in which boards operate and the accompanying complexity of issues being discussed by board members (Section 2.2), resulting in a growing recognition of the value of diverse perspectives and more inclusive cultures.

Indeed, one benefit perhaps of the shift towards virtual meetings in the wake of COVID-19 has been that of creating a fresh (and timely) opportunity to rethink collective engagement and participation. One sustainability consultant from the Netherlands reflected that the greater use of online meetings could enable more inclusive board dynamics.

> *"It allows people to ask questions in a chat as they go along. It allows people to raise their hand so it feels more … participative … whereas when it's in person, you can have a few voices who really dominate that conversation." (20)*

On the other hand, face-to-face meetings enable more awareness of body language, important in high-stakes decision-making contexts.

3.4.1.7. Challenges for board dynamics

The following challenges are expressed in terms of those dynamics and trends that are moving in a different direction from the observed trend that more attention is being paid to group dynamics and there is a shift to a more inclusive and independent culture.

It was noted that some of the contemporary pressures facing boards might be working against a move towards greater collegiality and inclusion:

> *"Boards are starting to struggle with the complexity of what they're dealing with. I think they're getting more and more tribal … now it's becoming just more – you've got to survive … you can't build trust and complexity and thoughtfulness." (12)*

There was a suggestion that the trend towards increased diversity may counter-intuitively lead to less open discussion. As one interviewee expressed it:

> *"We'll tolerate you. We'll tolerate your opinion … But you really don't understand what's going on here in our culture … And so boards get quieter because they don't want to offend." (19)*

Nonetheless, the fact that these issues were raised by interviewees reinforced the aspect of the trend that highlighted a growing awareness of the importance of group dynamics.

3.4.1.8. Trend trajectory of board dynamics

The shift in board dynamics away from one of passivity to inclusion of all voices and greater independence is likely to continue to increase. Key factors include the widespread adoption of the need for board independence among country regulators, its support within multiple governance codes, as well as generational changes in attitudes to hierarchy. It is likely though to proceed at different speeds in different geographies in line with the dominant culture of interpersonal behaviour.

3.5. Individual skills and interpersonal capabilities on boards

We turn now to our fourth and final thematic area of relevance to this domain: individual skills and interpersonal capabilities on boards. One of the most notable trends mentioned in the Global Trends Survey, as well as by about three-quarters of our interviewees, was a change in the kinds of skills, interpersonal capabilities and experiences that board members should ideally possess.

3.5.1. Trend 5: Increasing desirability of wider technical skills and knowledge, and more human and collegiate leadership skills

There is increasing attention being paid to the need for a wider range of technical skills and knowledge on boards, as well as growing appreciation of more inclusive and relational leadership capabilities. However, there are also concerns that these additional skills and enhanced capabilities are not being realised in practice to any great extent.

One interviewee, a reputation management consultant, summed up the general feeling that many boards are becoming increasingly more 'considered' about who they hire, not just in relation to diverse demographics:

> *"There is much greater effort … We need to know about technology … we need to have someone who is an expert in climate change, or whatever the range of skills or aptitudes the board has agreed … more process and thought and deliberation … to benchmark the skills of the candidates against the various capabilities the board wants to … demonstrate or … address." (27)*

Six main insights arose from our expert interviewees. These were:

- the increasing desirability of a wider set of technical skills and knowledge beyond those of traditional finance or business, but not at the expense of business acumen (Section 3.5.1.1)
- a growing appreciation for leadership skills that reflect the (changing) role and purpose of boards (Section 3.5.1.2)
- a growing appreciation for the 'human' side of leadership (Section 3.5.1.3)
- the importance of capabilities relating to creating constructive group dynamics, particularly with regard to the chair (Section 3.5.1.4)
- concerns about a current mismatch between desired capabilities and current board leadership capacity (Section 3.5.1.5)
- some reflections on how best to nurture these capabilities (Section 3.5.1.6).

3.5.1.1. A wider set of technical skills and knowledge required, but not at the expense of business acumen

In both the Global Trends Survey and expert interviews, a much broader range of technical skills and knowledge, beyond traditional finance and business expertise, was referenced as necessary for today's leadership. These capacities were acknowledged to reflect the changing business context and pressures raised in Section 2. The areas most frequently referenced in the Global Trends Survey can be found in Table 24, ordered by number of mentions by respondents.

Table 24: Technical skills or knowledge required on boards

Technical skill/knowledge (number of mentions)
ESG (53)
Sustainability (36)
Communication (33)
Diversity and inclusion (21)
Risk management (20)
Technology (18)
Change management (17)
Strategy (17)
Legal/compliance (14)
Financial management (13)
Digital (11)

These findings are only indicative, rather than definitive statements, of the kind of leadership skills and knowledge which are increasingly desired within board membership. As noted previously, the order here likely reflects the sustainability lens through which many of the respondents approached their replies. It is likely, for example, that 'traditional' capabilities around financial management and business expertise were assumed when answering the questions, rather than deemed to be less important. Indeed, one recruitment consultant from an executive search firm was clear what they as an organisation are not being asked for:

> *"We are not being asked for single issue directors … those individuals who are incredibly impressive and have an extraordinary amount of relevant domain expertise … but what they lack in a board context is just executive experience. You know, business experience, commercial acumen." (29)*

This wider expertise was noted to be particularly important in the context of ESG and sustainability, since the ability to integrate sustainability into core business as a compelling value proposition was seen as critical from this consultant's perspective. The outcomes of that activity will depend on whether this integration is alongside historical trends, or part of innovating a new way forward:

> *"It's someone who understands how to integrate a sustainability programme across an organisation and to frame it as a business value creation exercise, not a functional necessity or requirement, right? If you try to tell people we're doing this because it's the right thing to do, you're not going to get anywhere." (29)*

Research from The Conference Board and ESG analytics firm ESGAUGE based on an interactive online dashboard powered by ESGAUGE, as well as a focus group with leading governance professionals held in April 2022, suggest that, even though business strategy continues to be the most commonly cited experience for directors, the reported percentage of board directors with such experience has been declining – from 69.7 per cent in 2018 to 67.5 per cent in 2021 as reported in the proxy statement or other disclosure documents of the S&P 500. The Russell 3000 saw a larger decrease, from 67.7 per cent in 2018 to 62.9 per cent in 2021. The decline in strategic experience has been accompanied by a decline in international experience on boards as well – from 19.6 per cent in 2018 down to 14.4 per cent in 2021 in the S&P 500, and in the Russell 3000, from 10 per cent to 8.1 per cent. By contrast, experience in business operations, finance and technology in the S&P increased in recent years. This suggests that boards may be

attracting directors with knowledge in specific areas (eg cybersecurity) who do not have broad business strategy experience.[106]

Nonetheless, it was clear that a number of expert interviewees believed that a broader range of skills and expertise is now necessary:

> *"Have you got enough technicolor in that board rather than everybody looking quite similar in terms of skills that they can offer … finance and fiduciary duty specialists have always been valued on boards, and these other skills and these other areas of expertise are now equally important." (6)*

Interviewees also set out the range of skills and knowledge expected:

> *"But the new dimension of that is that in addition to having a very strong executive background, someone who's led a sustainable business transformation or someone who's come from a company best known for being best in class in terms of how they've integrated sustainability into their corporate strategy." (29)*

> *"…geopolitical issues … you need to know about the Sustainable Development Goals and climate, diversity equity inclusion [DEI], wellness, cybersecurity, responsible use of data, anti-corruption, integrity, tax, investment and pay. Some of the more traditional financials, but with more ESG lens." (11)*

> *"…understanding your people better … direct HR experience, people experience." (28)*

> *"…bringing in someone who's more knowledgeable and understanding of the latest IT landscape." (10)*

There was an implication that these new skills and knowledge were becoming part of board recruitment processes, and that they were felt to be more likely found within younger generations:

> *"[They are] looking for a different type of person coming onto the board that is much more aligned with generation Z and the millennials and ESG and sustainability." (22)*

There does not seem to be an expectation that all individual board members will necessarily be specialised in all areas, but that they will have a broad enough understanding of a wide enough range of skills necessary to be able to create effective challenge. For example, one interviewee noted:

> *"You want to bring someone in who is solid in cybersecurity, but that person needs also to be able to express an opinion when the discussion at the table is about a merger or an acquisition." (8)*

Table 25: Percentage of boards publishing skills and background of directors (2017–21)

	2017	2018	2019	2020	2021	2022
% of boards publishing skills and backgrounds of directors	94.1	95.3	96.1	98.2	100.0	(100.0)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

Globally, the Refinitiv Eikon data revealed that boards universally publish biographical data, including skills and background, on each of their directors. One hundred per cent of organisations in the global sample now give professional background information on each of their directors in their corporate literature – invariably on websites and in company reports – a figure which is up from 94.1 per cent in 2017.

Some interviewees cautioned that this resultant 'publicity spotlight' could be yet another pressure being put on today's directors.

3.5.1.2. Skills and knowledge requirements reflect the changing role and purpose of boards

The wider set of skills and expertise identified in Section 3.5.1.1 reflects the changing context within which boards and companies are operating.

Many expert interviewees identified specific leadership capabilities that would be desirable to enable the board to fulfil its role effectively.

These capabilities included, firstly, an awareness of the changing context and ability to identify the relevance for the strategic direction of the company:

> *"And the role of directors in ensuring that you serve this organisation in such a way that you, your commitment, is to the organisation's long-term sustainability." (13)*

> *"A much more dexterous agile multi-skilled kind of leadership role where you're having to have the antenna to spot and then absorb all of these … mega trends around the world and to then transpose those into your organisational context, and say 'What do these mean for us? What should we be thinking about for the longer term?'." (7)*

However, the latter interviewee reflected that there was a deficit in this desired capability – an issue discussed further in Section 3.5.1.5:

> *"I don't think business leaders at the board level, that I've seen, not many of them have those kinds of skills." (7)*

Secondly, a purpose-oriented, stewardship role was identified as a desired capability, to reflect business's broader role in, and impact on, society:

> *"What I'm hoping is that we have directors around the world, and leaders around the world, that see themselves as stewards – not only stewards of the financials, but stewards of the company [and] also stewards of the future, of the stakeholders that they are impacting." (11)*

A collaborative mindset was suggested as useful, one which is willing to co-operate with other organisations, rather than to *"be the best and to hell with the rest" (7)* mindset that has been traditionally dominant:

> *"I think that sustainability requires a different ethos. It requires partnership, sometimes between competitors or cooperation. It requires collective action across and between sectors, and that again requires a different mindset." (7)*

A 2020 report by Competent Boards, led by Helle Bank Jorgensen, explored what new competencies are needed for the future boardroom and C-suite, based on a survey of 100 board members, executives,

investors and experts representing a diverse range of industries and geographies, and working as faculty with Competent Boards. The report concluded that future-ready board members:

- will need to apply a lens of curiosity that supports a culture of continual learning and strategy adaptation in order to meet growing expectations
- should be aligned with a distinct sense of purpose that is informed by a deeply seated literacy of the material ESG challenges faced by the company
- might be defined by personal attributes or traits within their internal value system (eg courageous, empathetic, persuasive, entrepreneurial)
- should be willing to not only voice their own opinion but also engage with the opinions of others in order to avoid common boardroom biases such as groupthink
- leverage their power and influence to take meaningful action
- must reflect on their current outlook and set of competencies in order to identify areas for which they can develop their capacity to meet demands for extraordinary board-level stewardship in the 21st century.[107]

Russell Reynolds Associates published their work on 'next-generation board leaders' in 2022 in partnership with the United Nations Global Compact, based on an in-depth global study of 55 board directors and CEOs with a track record of successfully integrating sustainability into business strategy. They concluded that next-generation board leaders will possess the following four differentiating attributes:

- multi-level systems thinking – recognising the interconnectivity of the ecosystems in which their business operates
- stakeholder inclusion – considering a wide range of views and having high levels of empathy
- long-term activation – setting audacious goals and having courage and resilience to stay the course in the face of resistance
- disruptive innovation – challenging what has gone before, using the best available science to deliver for people, planet and profit.

Although not specifically about board leadership, CISL's latest leadership framework builds on an extensive literature review of over 350 academic and practitioner references, to identify the characteristics of leadership most likely to contribute to a sustainable future. The framework identifies a leadership 'purpose' – leadership that is in service of, and accountable for, a sustainable future; embedded in 'place' – leadership in context, whether geographical, cultural or historical; and characterised by four principles:

- connected – leadership that navigates the complexity and connectedness of life, and nurtures the relationships that underpin the systems on which we all depend
- collaborative – leadership that is inclusive and works in alliance with others across boundaries to achieve collective change

- creative – leadership that experiments and innovates with curiosity, optimism and purpose
- courageous – leadership that knows the values that it stands for and nurtures the integrity, resilience and commitment to pursue these.
- These characteristics are then used as the basis for identifying a series of mindsets and practices that can be activated at an individual and collective (team, project, organisational, partnership) level, and have resonance for individual board members and the board as a collective.[108]

3.5.1.3. A more human approach to leadership

When asked in the Global Trends Survey about the top leadership capabilities required over the next three to five years, alongside strategic thinking and adaptability, the most common personal qualities suggested were empathy, integrity and authenticity. These themes resonated with our expert interviewees:

> *"…we also need a heart … really putting ourselves into shoes of different stakeholders – empathy … to actually make sure that we not only talk about it but we actually do something." (11)*

> *"I think they have to be more human and more qualitative … I don't want to call them softer areas, because … they have very serious business implications. But the new leadership model is more authentic. It takes into consideration mental and physical well-being. It's more considerate of the impact and the footprint the decision is going to have, not just on the bottom line, but you know, on the ecosystem as a whole." (26)*

One interviewee reflected that these human dimensions were especially important with the development of AI, and enhanced data provision:

> *"…it's the … human skills that will make a difference … humans interacting in a condition that delivers good decisions, and good understanding, and creates value." (5)*

In addition, a number of interviewees referenced the importance of humility, which enables a greater ability to discuss complex challenges and seek appropriate information to help create solutions.

> *"I need someone that can say: 'You know what. I don't understand what you're saying right there. Can you explain that to me?'." (11)*

It was also recognised, however, that such humility – as with some of the capabilities referenced above – was sometimes lacking:

> *"It's very hard then to say, well, maybe I don't know the answer … if you're being paid £100,000 a year to sit on a board." (12)*

The *2022 Global Board Culture and Director Behaviors Study* undertaken by Russell Reynolds Associates, based on survey responses from 1,100 supervisory board-level directors from 41 countries (but with a European majority), seeks to identify the attributes of high-performing directors, dividing the insights into foundational or baseline characteristics:

- being prepared and engaged
- being current and open
- building trust and respect

- knowing their role (director rather than management)
- being stakeholder and investor savvy
- and then high-performing director attributes:
- applying sound judgement and relevant expertise
- engaging constructively and being willing to challenge management and peers when appropriate
- acting with integrity and courage
- asking the right questions and having focus
- possessing an independent perspective, avoiding groupthink and prioritising the interests of the company's shareholders and stakeholders.109

3.5.1.4. Leadership capabilities that support constructive group dynamics

In keeping with the trend for growing awareness of the importance of group dynamics (Section 3.4), a significant number of interviewees referenced the importance of leadership capabilities that nurtured more effective group dynamics. These included abilities to:

- listen well
- inquire and question in a constructive way
- be comfortable with difference and dissonance
- navigate conflict
- build trust, including between the board and management.

> *"…the ability to listen to one another, that's good for conversations, preserving the debate, preserving the contrast of different opinions and perspectives. These will make the difference in the future in my perspective." (5)*

It was acknowledged, however, that getting the right balance between different leadership capabilities, as well as a helpful tone and approach, can be challenging. For example, a willingness to challenge and question might be perceived as unsupportive:

> *"It's about the tone and the manner in terms of those board practices and dynamics that come across … And that often also contributes to the boardroom conflict that sometimes arises. You've got a board member … I've experienced this as well, a board member seemingly nitpicking on something … 'I'm looking. I'm providing oversight. I'm asking these questions.' In the meantime, management [sees] this as constant attack." (10)*

This builds on an insight already noted in Section 3.4.1.7 on challenges to board dynamics and the concern that greater diversity might lead to less open discussion.

The *2022 Global Board Culture and Director Behaviors Study* by Russell Reynolds Associates culminated in a framework called the 7 + 2 Model for Highly Effective Boards, based on the recommendation that in order to develop the most effective board possible, board leaders should look to assemble a group of directors who, as a collective group, always demonstrate seven behaviours:

- a board leader who focuses the board's attention on relevant matters
- a board leader who actively seeks different points of view
- directors who foster an inclusive culture
- directors who ask the right questions
- directors who use both a three to five year and over five year time horizon to evaluate opportunities and make decisions
- directors who are willing to constructively challenge management, when appropriate
- directors who actively cultivate a relationship with the CEO.
- It then added that a further two additional behaviours might be demonstrated, but "without going to extremes that can be problematic":
- directors who possess independent perspective and avoid 'groupthink'
- directors who actively cultivate relationships with fellow directors.110

Several interviewees referred to the need to manage their egos, be open to challenge and willing to learn:

> *"…can a leader step back from ego enough to have dissonance in a board to get to the best solution, or does a leader need to be affirmed all the time, and therefore stacks the board in his or her favour? That's a huge behavioural question, an organisational system question." (19)*

> *"…ultimately a board needs to make decisions, needs to make ethical and effective decisions. And that's made by human beings who come with egos into the boardroom … boards that work on those dynamics intentionally through different interventions of allowing people to connect with one another can be more effective … than someone who just gets appointed." (10)*

As already discussed, the role of the chair is especially important in setting the right tone, and creating effective space for discussion:

> *"I would say a lot depends on the chair … listening as well as telling and asking questions … everyone having a chance to speak, not shutting down people. I think some chairs are very good at doing that, and … leaving space for many different views to be heard." (20)*

3.5.1.5. A deficit in skills and knowledge among current board members

A deficit in skills and knowledge among current board members was mentioned in interviews in at least three different ways.

The first is that, although there is a trend towards boards desiring a wider set of technical skills including ESG and sustainability expertise, and more inclusive and relational skills, not all firms and boards share this perception, or want such capabilities. The following quote is from a recruitment consultant for an executive search firm operating in the US, reflecting on the proportion of firms requesting board expertise around ESG and sustainability:

> *"Most boards recognise the need to raise their level of domain expertise around ESG and sustainability … I don't have hard data so this is a guess, I would say between 25 and 50%, but it's rising; the trend is positive." (29)*

And in terms of the 'social' dimensions of sustainability in particular:

> *"So I would say we're pretty well behind our global colleagues and in terms of the adoption of that as a required dimension or even desired, no not really." (29)*

Second, a number of expert interviewees commented that the kind of leadership capabilities and skills that are desirable and necessary to manage current and future challenges are not necessarily those that board members would have developed as a result of traditional board backgrounds (such as legal or finance, or being a successful CEO or senior executive).

One interviewee, a governance academic and consultant, asked:

> *"What leadership skills does the board director bring? … The business as usual model … [is] someone who has been there, and done that, and got the T-shirt – who'd run a business, done it well and had enough experience … That traditional route to board membership is problematic because it tends to support and encourage 'business as usual' as opposed to a very different way of thinking about the role of a business organisation in our current human predicament." (7)*

This feeling was echoed by a UK-based sustainability data expert:

> *"Many people who sit on boards are people who have successfully run businesses and have successfully driven change and made a big difference. But they've made that difference in yesterday's world." (15)*

A further UK-based interviewee reflected in a similar vein:

> *"You know, you're asking people who are trained to do one thing, which was make a trade or a deal which makes the biggest profit for our business, and you're now asking them to make huge decisions with all manner of factors in the background, which they were never educated to, or put pressure or incentivised to do. And the board needs to understand that." (17)*

The call for different leadership capabilities to address current and future challenges relates to the earlier discussion around board diversity, with a particular focus on age and experience:

> *"…the average age of board directors in the US is mid 70s and … not many of those folks grew up in a sustainability ESG kind of world … You're going to be targeting, you know, demographically younger people to fill director roles." (29)*

The NYU Stern Center for Sustainable Business assessed the credentials of 1,188 Fortune 100 board directors and found that only about 1 per cent possessed expertise in any environmental field, including energy, conservation, climate and sustainable development.[111]

Third, where there is appetite to recruit new members, it was noted, however, that there is the need to develop the pool of potential board candidates:

> *"All boards are taking meaningful steps to increase diversity, but it will take some years for a deep pool of diverse NED talent to emerge. Finding ways to support and develop this is important." (Global Trends Survey)*

Finally, upskilling existing board members presents its own challenges. A number of interviewees noted the pressure that rising expectations placed on the capacities of existing board members, although it was acknowledged that this might open up opportunities for a new generation of board members:

> *"And I think that's where they're really struggling … some directors have said to me: 'We're trying to keep up with everything that's going on and all the changes, but it's difficult' … they're not starting with a shared understanding in the boardroom in terms of how people see their duties." (21)*

> *"It's becoming harder to be a board member, and that's not a bad thing … We now have the great resignation of employees. Will we also see the great resignation of board members?" (11)*

A 2020 article in the *Harvard Business Review* recognises this board push to widen the talent pool, but points out that the bar for 'board readiness' has never been higher, given all the regulations and expectations on today's boards. The silver lining for people from non-traditional industrial backgrounds, they point out, is that the capabilities needed to be a board director today are not in fact those needed to operate at an executive management team level. As the authors said: "Stepping up to the board requires you to take a step back. The role is to scrutinize, encourage, and advise, not operate".[112]

3.5.1.6. Filling the gaps in capabilities

Interviewees talked about two strategies for nurturing the required leadership capabilities: the first being to refresh the board by recruiting new members who bring a wider set of skills and capacities; the second around training and upskilling.

Several interviewees felt that as a result of the currently desired skills and capabilities, there is more rigour in how directors are recruited and balanced.

> *"There's much more process and thought and deliberation … and attempts to benchmark the skills of the candidates against the various capabilities the board wants to be able to demonstrate, or wants to be able to address." (27)*

In a recent contribution to the Harvard Law School Forum on Corporate Governance, executive search firm Russell Reynolds Associates argued that making a sustainability mindset – and not simply sustainability expertise – a factor when hiring directors was a key. The authors argued that it was essential to "look for great directors who believe business isn't divorced from wider society and who can align all they do to sustainability".[113]

There is also deliberate investment in upskilling current and potential board members:

> *"It's like management. People just get promoted and they go up the organisation and are expected to know how to be good managers, but no one ever teaches them. I think the same goes for boards." (28)*

In Singapore, recognition of the lack of understanding of sustainability by board directors resulted in mandatory training in 2022 for listed companies on the Singapore Exchange.[114]

The pioneering board governance thinker Bob Garrett forecast 20 years ago in *Thin on Top* that directing could itself become a recognised profession, incorporating a wider range of benchmarked skills than had

been the case in the latter part of the 20th century.[115] He characterised a 'learning board', where directors constantly sought to improve their skills and capabilities.

A related approach to considering the most appropriate balance of refreshing the board, or training and upskilling existing members, was suggested to be that of using competency metrics to more formally assess current and future competencies:

> *"The companies that are more mature in governance are using competences matrices to have a structured manner to analyse what are the competencies needed for the board, what are the characteristics of the directors, how [convergent is it] with the strategy of the company?" (5)*

3.5.1.7. Drivers of trends in individual skills and capabilities

One of the main drivers for this trend is the good practice expressed in corporate governance codes that boards should have a combination of skills, experience and knowledge.

The interviewees also referenced the recognition that improved skills and competencies lead to better decision-making, particularly in a rapidly changing world, reflected in the many surveys of skill needs that have been presented in this section.

This has prompted a growing sense that the current generation of board directors does not possess the required knowledge, expertise, mindsets or capabilities to respond to megatrends facing contemporary business, from digital transformation to diversity and inclusion.

In a recent report by the US executive search firm Russell Reynolds Associates on the next generation of board leaders, Paul Polman is quoted as saying: "Today's boards are just not equipped to deal with today's challenges. They don't reflect the real world anymore. The world has moved on, and, frankly, many of the boards have not moved on in ESG … and climate knowledge. We have a problem … that with the urgency that we need to act right now, boards might become a bottleneck."[116]

3.5.1.8. Challenges to changes in individual skills and capabilities

The difficulties associated with desiring this widened set of skills, experiences and capabilities among board members are similar to the challenges of diversity in terms of the danger of 'box-ticking' candidates, and a lack of suitable candidates. It also seems from the insights of our Global Trends Survey and interviews, that there is more of a reactive approach to incorporating more skills and knowledge in response to external and current demands, rather than one which is considered.

Additionally, it was felt that there was a lack of training to provide additional skills to those already on boards.

As one interviewee reflected, there are:

> *"…more traditional skills that you need as a director. And then there's sustainability … But there isn't any training to help directors actually bring those two responsibilities together. (21)*

In fact, there are a number of established and emerging board education programmes, as well as bespoke training programmes for individual firms and resources designed for individuals and boards, that focus on building individual and collective capacity in board leadership for sustainability. This quote, however, appears to speak to a lack of awareness of available training, programmes and resources in this area.

There are examples of board leadership training emerging that seek to build board leadership in response to sustainability challenges and opportunities:

- The Earth on Board programme aims to equip board directors to challenge and guide management and form strategic responses in relation to sustainability trends.[117]
- CISL offers a portfolio of board education programmes designed to develop the skills and mindset to enable the board to provide the direction and oversight that the company needs to secure its long-term resilience, while contributing purposefully to human wellbeing and a thriving economy.[118]
- Russell Reynolds Associates and MIT Sloan School of Management co-launched a sustainable leadership programme in 2022 designed to equip C-suite executives to pivot their organisations to a sustainable future.[119]
- The Institute of Directors has launched a course designed to equip directors with the knowledge and skills to strengthen their organisation's orientation towards sustainability.[120]
- The UN Global Compact Board Programme seeks to align and support boards of directors to effectively oversee and drive a strategic approach to corporate sustainability, and to respond to the interests of all key stakeholders while protecting and creating financial value.[121]
- IMD's Driving Sustainability from the Boardroom programme in partnership with WBCSD aims to equip directors in their role of influencing and steering the integration of sustainability into their company's strategy.[122]
- A 2020 report by Competent Boards explored new competencies needed for the future boardroom and C-suite.[123]

3.6. Board membership, structure, dynamics and skills: concluding reflections

From the trends identified in this section, four key themes emerged: board composition, board independence, board structure and board performance. Each of these is discussed here, reflecting on their potential meaning for board practice, and tentatively suggesting implications for business sustainability using the lens of the three logics of BAU Corporate Social Responsibility (CSR), Enlightened Shareholder Value (ESV) and Purpose driven.

3.6.1. Interim conclusions on board composition

Board composition is a key area of board practice where we identify converging trends around rethinking the make-up of boards, particularly in response to the complex strategic environment in which boards operate, as well as changing norms around diversity and inclusion. Assembling and leveraging a diverse board is a core theme that emerges from our analysis. The evidence shows a steady, albeit slow and geographically varied, trend towards greater representation of women and ethnic minorities on boards. It appears, however, that far less attention is being paid to other aspects of diversity, such as cultural and cognitive diversity, disability, age and experience. Additionally, the number of board directors from countries other than that in which a company is headquartered (as one measure of cultural diversity) is static globally, but varies by geography and sector.

Board diversity is a way to ensure that the company inclusively represents its shareholders, workforce and customer demographics. Board diversity has also been seen as a corporate governance safeguard against the groupthink that can breed complacency and inertia, stifle innovation, and prevent the board from alerting the management about emerging opportunities or risks. As jurisdictions around the world begin to enact laws and regulations regarding board diversity, companies with wider board representation are better positioned to meet these evolving regulatory norms, and can also enhance their reputation with stakeholders.

On the other hand, our data suggests that more diverse boards can also potentially lead to increased interpersonal friction, less cohesive collaboration, and slower decision-making, especially if not effectively managed. The role of the board chair is therefore crucial in facilitating inclusive dialogue and ensuring that a diverse board is more than just the sum of its parts. Furthermore, tokenistic diversity can leave some board members feeling disenfranchised, limiting their contributions to board discussions. As boards become more diverse, a key challenge is therefore to reframe diversity as a strategic resource to be leveraged for improved decision-making and risk management, and improve ways of harnessing this diversity, rather than seeing it merely as a quota-filling, tick-box exercise.

3.6.2. Board composition: implications for business sustainability

If diversity is a strategic resource that can be leveraged for improved decision-making and risk management, how can it also align business success with a sustainable future? Analysing the relationship between board diversity and sustainability implications is not straightforward. The relationship is nuanced and multi-layered. There is no automatic correlation between greater diversity and positive sustainability outcomes, although there are clear indications that this is an area worthy of further research.

There is some evidence that a board's overall diversity, particularly relating to gender, might be linked to positive sustainability outcomes.[124,125] Such research, however, is strongly influenced by what is meant by 'sustainability outcomes'. There is far less empirical research regarding ethnic and cultural diversity. Further insights in this area will be needed to avoid making simplistic associations between diversity characteristics and sustainability, as a result of each diversity 'category' overlapping with other demographic dimensions such as socio-economic status and class.

In the absence of this greater understanding, we have therefore used our findings to generate interim propositions for how board diversity could relate to sustainability outcomes, in order to inform further empirical work in this area, whether by ourselves or others.

3.6.2.1. Equity matters in and of itself

Board diversity arguably has intrinsic value in terms of sustainability outcomes. Equity is a core part of any holistic view of sustainability, aside from its impacts on business performance. It is, for example, a cross-cutting issue that runs through the achievement of the Sustainable Development Goals, as well as being a specific goal.[126] Whether or not equity, and the intrinsic value of diversity, is appreciated by a company and its board is very likely to depend on its logic or approach to sustainability. Using our sustainability framework, we can suggest the following implications for boards adopting different approaches:

- Business-as-usual CSR approach. Likely to be driven by legal imperatives, the interests of powerful stakeholders, and concerns with short-term profit maximisation, rather than equity for its own sake.

- **ESV approach.** May go beyond legal requirements, especially if pursuing diversity on equity grounds, aligning with current and likely future societal values. It is therefore a potential driver of long-term financial value for the company.
- **Purpose-driven approach.** The most likely to pursue equity through diversity for its intrinsic value.

3.6.2.2. Board diversity has practical value to help achieve sustainability outcomes

Board diversity has potential utilitarian value related to its ability to better achieve sustainability outcomes, although this relationship is multi-faceted and complex. For instance, an individual may tick a particular diversity box because of their background but may not be able to represent the views of that constituency. Equally, an individual may bring gender or ethnic diversity, but not cognitive or intellectual diversity, since they have a similar background, education, experience or training to other board members. And even in terms of cognitive or intellectual diversity, there is a difference between a board having diversity in mindset and ways of thinking, and a board having diverse and inclusive information to inform their decision-making.

Notwithstanding these nuances, we suggest that a more diverse board composition could give rise to a broader range of perspectives and worldviews, equipping boards to navigate more effectively the complexity of contemporary sustainability issues, and to respond proactively to the megatrends influencing the current business context. As a South African governance academic reflects:

> *"We're dealing with enormous complexity. So you need different viewpoints to untangle that complexity." (7)*

This attention to diversity may also involve accessing insights from a broader group of stakeholders – particularly parts of the operating environment that might otherwise go unseen – therefore providing a richer insight into the places and people impacted positively or negatively by sustainability issues.

To counter groupthink, we also propose that a more diverse board membership could be more willing to question, challenge BAU, and tackle vested interests, essential to transforming otherwise unsustainable trajectories.

> *"You're invariably taking on business-as-usual. You're taking on powerful vested interests. You're taking on significant interests in the status quo, maintaining the status quo. So you need people around the table who are willing to challenge that to ask, attack it from different angles. And that's where diversity, I think, is potentially very powerful and probably essential to creating real sustainability leadership at board level." (7)*

There is evidence that organisations driven by all three logics – business-as-usual CSR, ESV and Purpose driven – recognise the importance of board diversity. What is critical, however, is the diversity of information with which the board engages, and how this information (whether knowledge, worldview or ideology) impacts on its decision-making. We suggest that this dynamic is fundamentally shaped by the board's understanding of the organisation's reason to exist:

- **Business-as-usual CSR approach.** Companies are constrained by the overriding pursuit of short-term financial returns, and are therefore less likely to shift their dynamic proactively in order to engage insights arising from their board's diversity, and may be less diverse in the first place.

- ESV approach. Some companies are likely to recognise the value of multiple perspectives and mindsets to help understand and devise strategy which is focused on contributing to the maintenance or enhancement of underlying social and environmental capital.
- Purpose-driven approach. This is the only logic likely to respond in a deep, purposeful and transformative way to pursuing overall wellbeing for people and planet. As such, it is likely, if steered by a committed chair, to incorporate a dynamic of full inclusion and recognition of the relevance and importance of diversity, as well as the creation of processes to ensure its realisation.

It is, however, possible that the diversity in board composition driven by a CSR logic may still harbour the seeds of transformation as board members are exposed to a broader range of worldviews and ideologies. This potential, of course, assumes that the group dynamics of the board enable this diversity to be 'heard'.[127]

3.6.3. Interim conclusions on board independence

Clear evidence shows a consistent trend towards an incremental increase in the number of independent NEDs serving on the boards of listed companies. Independent directors have long been associated with better board oversight, and are often favoured by regulators, who perceive them as effective intra-firm governance gatekeepers.[128] Intuitively, independent directors are well positioned to provide more impartial views on corporate matters, keep management in check, balance power dynamics in the boardroom, and ensure prudent risk-taking. Independent directors are also expected to protect the interests of minority shareholders, particularly in companies with concentrated ownership, and to promote greater corporate transparency that serves stakeholders' informational needs.

Given that board independence is a widely accepted benchmark of good corporate governance, companies with a high proportion of independent directors are also associated with greater investor confidence, improved risk oversight and a lower cost of capital. Independence, however, is not only a formal status. It is a mindset, a capacity to exercise autonomous judgement and make context-specific decisions that align with a company's overarching purpose and strategy, while resisting pressures and inappropriate influences. Independence is therefore expressed across various dimensions of a corporate framework: from an individual director's independence from board colleagues, to the chair's independence from the CEO, and the board's independence from executive management or influential stakeholders. It is an essential trait that enables effective board dynamics.

The trend, however, towards more independent NEDs on boards also means that there might be fewer directors with operational knowledge of the company. Since NEDs do not participate in the day-to-day running of the company, they may not fully grasp the intricacies of its operations, or the specificities of the industrial sector. This lack of experience can result in a disconnect between the board and the management team. Furthermore, critics have argued that independent directors can be inefficient monitoring agents, lacking a substantial personal stake in the long-term success of the companies in which they serve, having little company-specific commitment.[129] Even when the commitment to the company is strong, exercising the monitoring function effectively relies on information controlled and supplied by corporate managers, which limits independent directors' oversight capabilities.[130] Effective oversight by independent directors requires clear protocols for information access and direct channels of communication with key personnel (as well as providing a clear opportunity for the smart use of technology).

3.6.4. Board independence: implications for business sustainability

As with the relationship between diversity and sustainability outcomes, the relationship between board independence and sustainability is complex and nuanced, and there is limited empirical research in this area. In fact, we would suggest that there is no a priori reason why board independence will have any effect on sustainability outcomes, but we have used our findings to generate a series of propositions for how board independence could relate to sustainability outcomes under certain conditions, with a view to informing further work in this area.

Independence is a relative term; it is defined as freedom from the control or authority of another, and is often described in relation to a prevailing norm or practice. Understanding its implications for sustainability therefore requires an articulation of what goal or parameters a person or entity is independent from, and indeed what alternative goal or parameters are being pursued through that independence. As has already been acknowledged, a dynamic of independence can operate at different scales – from interpersonal relationships within the board, to the relationship between the board and other entities such as key stakeholders. It can be used in the sense of formal separation of roles and responsibilities, or the sense of a culture, habit of mind, or 'spirit' of independence, characterised by a willingness to challenge BAU, ask difficult questions, and be willing to confront engrained norms, power dynamics and assumptions.

We propose that independence in the sense of a clear distinction between the role of the board vis-a-vis the executive could enable a board's unique responsibility to provide robust direction, oversight and accountability, informed by, but not immersed in, operational detail. Whether that direction, oversight and accountability is in service of sustainability outcomes depends on the logic adopted by an organisation: the short-term shareholder financial maximisation of the CSR logic, the long-term shareholder financial value of the ESV logic, or the strategic contribution to long-term wellbeing for all at the core of the Purpose-driven approach.

It is difficult to be clear on the optimal split of non-executive and executive positions in relation to achieving sustainability outcomes. Executives are closer to the 'action' and more likely to understand how any changes will be implemented. They can therefore push back on ideas which may be impossible or even 'reactionary' (in the situation that non-executive members are operating with little knowledge of current good practice). This can result in a disconnect between the board and the management team.

This dynamic tension may be particularly important when undertaking sustainability transitions, and it is likely that this area would benefit from further research into how a board might be both independent enough to provide effective oversight and accountability, while remaining close enough to the operational detail to oversee the complexities of transition and change towards being more sustainability focused.

We also propose that independence, in the sense of a willingness and ability to tackle vested interests and power dynamics, and an appetite for challenge and disruption, might be critical for aligning an organisation with sustainability outcomes, especially when those vested interests are bound up with BAU and unsustainable trajectories:

- Business-as-usual CSR approach. There is likely to be significant alignment between BAU vested interests and the interests of the board. Challenges with regard to sustainability that do not enable or support short-term profit maximisation are unlikely to be accepted.

- ESV approach. A culture of independence is critical to being able to step away from short-term pressures, and the views of those applying such pressure.
- Purpose-driven approach. A dynamic of board independence is likely to be critical in opening up space for more creative debate and discussion around the strategy and supportive practices for an optimum strategic contribution to long-term wellbeing for all.

The relationship between this culture of independence and the prevalence of truly independent NEDs on the board is another area for future enquiry. NEDs can provide informed and independent advice and requisite challenge, but of course, independence can cut both ways. The presence of a NED holding to a BAU position on an otherwise aligned and Purpose-driven board may be disruptive and challenging but in a different sense. That said, well-chaired debate and discussion which draw on a diversity of perspectives to reach robust and rigorous positions could help align an organisation with sustainability outcomes and would be a hallmark of a well-performing board.

There is also a need to further explore the tension between the gain in terms of 'independence' as a result of shortening board tenure and increased turnover of board members, and the implications for the sustained commitment often necessary in any kind of sustainability transition, which could be diluted through constant change.

3.6.5. Interim conclusions on board structure

Ensuring the optimal design of board structures is a precondition for board effectiveness. However, the most effective way of doing so is subject to ongoing debate. The size of a board, for example, can have immediate governance consequences. Ideally, board size should strike a balance between a broad reservoir of skills, agile decision-making, and the ability to understand and reflect the views of the range of material stakeholders. A larger number of directors can bring together a more varied group of individuals, thereby also tapping into a deeper pool of skills and expertise. Such expansive boards can more adeptly handle increased workloads. A potential trade-off, however, is that larger boards may face slower decision-making processes, and reduced rates of director engagement.

Our evidence indicates that board structures are changing with a proliferation of sustainability-related committees. (However, it needs to be noted here that this analysis primarily draws on data from publicly listed companies that have had sub-committees for several decades. This tends not to be the case to the same extent for private unlisted businesses.) This decentralisation of board activities can enhance board effectiveness by enabling a more granular focus on company-specific complexities; optimising task allocation; improving information gathering; engaging individual directors more actively in board processes; and signalling enhanced board attention to emerging trends. By improving knowledge specialisation, information production and director participation, sub-committees can also provide better decision-making, oversight, advising and accountability. Conversely, compartmentalisation of issues through sub-committees may result in information silos.

These divisions may hamper board dynamics and decision-making if critical knowledge is not adequately disseminated to the entire board, or if power dynamics lead to the strategic withholding or manipulation of information to gain situational advantages. Hence, ensuring that sub-committees have clear and delineated mandates, information circulation protocols, adequate staffing and cross-functional co-ordination are key to meeting company needs.

3.6.6. Board structure: implications for business sustainability

As with the other trends in this domain, there is no single definitive relationship between board size, structure and sustainability outcomes; much is dependent on context. There therefore needs to be more research across multiple contexts to generate more nuanced insights. Nevertheless, our findings highlight some different aspects worthy of further practical consideration.

The optimal size of the board depends on the number of sub-committees, and other aspects of governance. It is also intimately tied to the desired goals and success metrics of the company – in other words, what is being planned, and for what purpose? We suggest that, in light of the trend towards greater board diversity, and the sheer number of complex challenges facing contemporary boards, a board at the lower end of what we have found (about six or seven) seems to be too small to tackle this increased number of responsibilities, while providing direction, oversight and accountability towards a sustainable future.

In terms of sub-committees, the tension already noted between focused attention and knowledge-specialisation versus integration and co-ordination across all core activities is a live issue when thinking about the ability to align with sustainability outcomes. The interviewees were unclear themselves, and also in relation to the boards of which they were aware, whether or not a separate sustainability-related committee is the best approach, compared with incorporating ESG/sustainability issues into other committees (such as risk, audit or nomination) or, alternatively, whether it is better to adopt both approaches simultaneously. The presence or otherwise of a sustainability-related committee is therefore not in itself a definite marker of a company's full commitment to ESG or wider sustainability goals. The relevant knowledge and discussions may be incorporated at an all-board level, or be part of the agenda of other sub-committees.

While, on the face of it, the rise in sustainability committees suggests more commitment to sustainability outcomes, it is also impossible to know if this trend means that sustainability issues are being effectively incorporated into board decision-making, or impact on deeper discussions about board purpose, and value creation. Equally, as we have seen, the absence of a sustainability committee does not necessarily signal a lack of attention to sustainability issues. It may be the case that a sustainability sub-committee is a stepping stone to its complete incorporation as a priority area by a board, or the incorporation of ESG/sustainability issues into other committees. For example, the audit committee might oversee ESG reporting and disclosure requirements; the risk committee could look after environmental risk management.[131] One interviewee, a reputation management consultant, expressed their view on the current situation:

> *"Some boards would still be using their Audit and Risk Committee to look at the whole picture and this expanded picture around sustainability and risk and opportunity. But others will be putting together and creating a separate ESG or Sustainability Committee which can help to direct and manage the duties of the board around those particular risks." (6)*

We suggest that the relationship between the existence of a sustainability sub-committee and a company's ability to better create positive sustainability outcomes will depend on the logic adopted:

- Business-as-usual CSR approach. A relatively cosmetic approach could result from solely being driven by legislation and regulation. The actual impact will depend on the terms of reference of any such sub-

committee, but in general, by marginalising this function, it could risk failing to appreciate the systemic effects of the challenges posed by sustainability (for example climate change) or the impacts of sustainability transitions on the business.

- ESV approach. A sustainability committee could allow focused time and attention on the ultimate means (natural and social capital) on which the organisation and wider system depends. The ultimate effectiveness of this sub-committee will depend on whether or not it is acting as a catalyst to embed change in the business.
- Purpose-driven approach. It may be unlikely that such a company would have a specific sub-committee focused on sustainability, given that this function permeates all aspects of the board's remit and function. There is certainly a need for more detailed research into how a Purpose-driven company might best design the most appropriate sub-committees, and balance these activities with the overall responsibilities of all board members to most effectively contribute to the achievement of the purpose.

The nomination committee is thought to be the most important of the sub-committees by the Corporate Governance Institute.[132] This situation has changed markedly from previous years where the nomination committee tended to be far less important than the audit or remuneration sub-committees. Clearly, the ability to affect who is recruited, define what success looks like, and manage performance, could have considerable implications for sustainability outcomes, both positively and negatively. Again, we propose that the alignment of the observed trend in nomination committees with sustainability outcomes depends on the prevailing logic.

- Business-as-usual CSR approach. Alignment of the nomination committee's activities with sustainability is unlikely since sustainability issues are not seen as important to the board or CEO.
- ESV and Purpose-driven approaches. In both logics, boards could see the benefits of the role of the nomination committee in recruiting the best composition of board members, and a CEO with appropriate capabilities (as discussed later). It has been argued that this sub-committee could also focus on ensuring that the company's purpose and strategy aligns with the board's functions and capabilities.[133]

3.6.7. Interim conclusions on board performance: dynamics and capabilities

The composition and configuration of the board also influences how board members interact and work together, which in turn affects the dynamics within the board. Our ongoing research suggests that there is growing awareness of the importance of board dynamics, which is partly reflected in what appears to be increasing numbers of board evaluations. As more companies undertake board evaluations, or express intentions to ensure the independence of their boards as a precondition for board performance, these moves reflect a desire for balanced decision-making and effective oversight. Companies are also recognising the benefits of delineating the chair and CEO positions, fostering a culture of checks and balances, and allowing for a more balanced distribution of power within the board.

If we delve more deeply into the mechanics of board dynamics, there seems to be a shift from hierarchy to collegiality, signifying a potential move towards more collaborative and inclusive decision-making. Maximising a board's independence and diversity as a strategic asset for corporate performance requires

board leadership. The skills of the chair – their leadership, communication, facilitation, conflict resolution skills and relationship-building skills – seem to have therefore emerged as a key determinant of board effectiveness and overall group dynamics.

Although the emphasis on the impact of board structure, group dynamics and directors' skills on board effectiveness increases, key difficulties remain about how to link a company's outcomes with board performance. By what ultimate objective, or objectives, is effectiveness evaluated, and on which criteria is that performance measured? Ultimately, the parameters of board effectiveness and performance measurement are framed by the board's purpose, and the expectations of its key stakeholders.

Improving board performance also depends on the skills and capabilities of individual board members. Our evidence shows an increasing appetite for diversifying the available pool of technical skills and knowledge available on boards, and a preference for professionalism, independence, effectiveness and collegiate leadership conducive to more inclusive and collaborative decision-making. The demand for these new skills and knowledge capabilities reflects the changing role of boards, the need to upskill existing members, and build a pipeline of talent to ensure that succession plans respond to evolving skill gaps.

3.6.8. Board dynamics and capabilities: implications for business sustainability

Amid the growing emphasis on board performance and effectiveness, the question remains of whether such a focus will actually deliver sustainability outcomes. The answer revolves around clarity over what counts as performance, and what the desired objectives are against which effectiveness is evaluated. There are different responses – from maintaining BAU (and the tactical compliance for reputational reasons found in a CSR logic), to enlightened forward-thinking for the long-term shareholder value of the company (ESV), to a Purpose-driven commitment to contribute strategically to long-term wellbeing for all. These different approaches will shape expectations around board performance and effectiveness, which in turn will shape intentions and decisions around board evaluations, and what is desirable in terms of dynamics and capabilities.

3.6.8.1. Board evaluations

While board evaluations are not necessarily aligned with positive sustainability outcomes, they could become an important enabler, benchmarking a company's sustainability performance against their peers and diffusing best practice.

Through a deeper understanding of the various trends identified in this report, board evaluators could also provide effective insight into board practices and dynamics that could support the organisation in shifting from a CSR to an ESV, and to a Purpose-driven logic, and help hold it accountable for that dynamic journey.

As one interviewee – a governance consultant based in the UK – reflected, an external board evaluator might ask:

> *"Why have you not got a sustainability report or if you have got a sustainability report, why have you not integrated it into your annual report so that you've got an integrated report? Those sort of questions are now being [asked] … an external evaluator who is doing that sector or knowledgeable*

about that size of organisation, and so on, is able to compare with other organisations and say well, your competitor X has done this … why haven't you?" (22)

This response, however, hints at an ESV approach, rather than the likely additional requirements of being Purpose driven. With the latter perspective, a board evaluation would focus on whether, and to what extent, the purpose itself was being realised, as well as whether the processes employed by the board were acting supportively to achieve that objective.

3.6.9. Skills and capabilities

Over the last couple of years, there have been growing calls for more attention to be paid to the leadership capabilities and qualities required at an individual and collective level to make fundamental and sustained progress towards a sustainable future.[134] Frameworks such as the Inner Development Goals have emerged to complement the Sustainable Development Goals, articulating the inner capacity to deal with our increasingly complex environment and challenges.[135] As CISL's own work in this area has articulated,[136] alongside the work of others,[137] nurturing a mindset (a way of thinking and being) and associated practices (the skills and sense of agency) at both an individual and collective level is critical for building leadership capacity in service of a sustainable future.

When it comes to board leadership, the need to recruit people with business acumen, with experience in the company's particular sector, or from legal or finance backgrounds, is unlikely to disappear. The trends towards recruiting and training board members with a broader range of capabilities that include: different technical knowledge (for example around ESG and sustainability); the human dimension of leadership; skills that foster effective group dynamics; and a broader range of experience and perspective, may well help to equip boards with the capabilities needed to support businesses to align themselves with a sustainable future. These capabilities include bringing the richness of multiple perspectives to the VUCA context in which business operates, and the independence of thought necessary to challenge BAU and tackle vested interests. Appropriate skills and knowledge on the board may also enable executives who are already ahead on the sustainability agenda to interface better with the board.

"The chief sustainability officers are still struggling to get it on the radar … helping them to understand the enterprise risk register … helping them particularly to throw opportunities to the board because that's the language that boards work with day in, day out, is a key way to get on the radar … the entry points that can help educate and influence and motivate a board to act and change." (15)

The key question, however, is whether the trends observed to date will be sufficient to result in the collective capacity to lead transformative change, or whether boards will need to invest more intentionally in building the courage, vision, culture and behaviour to align profitable business models with a social purpose of long-term wellbeing for all. As governance expert and Director of CISL South Africa reflects:

"In boardroom terms, how many of us who serve as directors hold something back? My sense is that some directors are 'diligently coasting' – that is to say, they are doing what is expected of them but coasting relative to what is needed from them. They turn up and serve respectably, donating their accumulated years of experience and expertise, but not taking that additional step that is the hallmark of true independence: the willingness to pose the really difficult question and to challenge even the holiest of cows."[138]

It was recognised in the interviews that any board that is committed to moving towards an ESV, and particularly a Purpose-driven approach, is going to have to pay particular attention to ensuring that their strategy for board appointments, training, assessment, and pipeline development is proactive in ensuring the right mix of skills and capabilities, rather than being reactive, as we have seen is mostly the case.

- Business-as-usual CSR approach. Boards adopting this logic will need to increase their ESG skills to better oversee compliance duties in this area.
- ESV approach. The company's general commitment to ensuring the maintenance and enhancement of social and environmental capital may require additional sustainability experiences and skills beyond that of CSR.
- Purpose-driven approach. Boards operating with this logic, or committed to making the transition to being so, are likely to require a level of transformational leadership skills and strengths that are higher than those needed for ESV.

4. Purpose, strategy, materiality, disclosure and stakeholder engagement

The second set of domains of board practice to be discussed are those concerning organisational purpose, strategy, materiality, disclosure and stakeholder engagement (originally conceived as Domains 2 and 4 in our research design). These five areas are strongly interrelated. Material considerations, for example, inform what is and should be disclosed, and organisational purpose is the overriding objective which guides any strategy being devised. The different kinds of information which are collected by an organisation inform internal processes, as well as strategy design, are a way to assess whether an organisation is indeed fulfilling its purpose and communicate the findings to stakeholders. Stakeholder engagement, including with shareholders and investors, is a crucial part of materiality and reporting considerations, as well as their knowledge being valuable to strategy creation.

The overall research design we adopted for the Future of Boards research was created in order to determine general trends, and then explore the extent to which they align with sustainability outcomes. However, while we followed this approach for Domain 3, this linear analysis is harder to use for Domains 2 and 4. The concepts of 'materiality' and 'purpose' have themselves evolved precisely in order to better align companies with sustainability outcomes, as have changes in what is reported and disclosed.

A core question for this part of the research is therefore the extent to which boards are responding to, and adopting, these different understandings, and the implications and challenges of doing so. Materiality, for example, may or may not be linked with sustainability, depending how it is understood and defined, and its use is in turn shaped by the underlying rationale for the business (in other words, whether it has a CSR, ESV or Purpose-driven approach).

One overall insight from our interviews was that board members themselves seem to be unclear about what to do in this evolving situation. Their responses suggest that we are in a time of rapid change in thought leadership and good practice, but one which is also creating a lot of confusion.

An additional challenge is that most of the secondary literature we accessed across these five areas had a primary focus on management practice, rather than on board responses and insights.

At this stage of our research, we therefore draw primarily on the comments made by our interview respondents. Their thoughts give us indicative areas for further exploration. We support these insights from secondary data – primarily academic and practitioner-oriented literature – and include some limited data points from the Refinitiv Eikon data, as well as the Global Trends Survey. Further and deeper analysis into some of these areas will be undertaken in Phase 2.

As a result, unlike for Domain 3, it is difficult to talk about specific trends, and how they are playing out among boards, with any certainty. In the discussion that follows, we therefore do not include specific sections on drivers and challenges, or on specific alignment with the sustainability framework. Rather, we leave comments on the implications of these trends for sustainability to Section 5, Conclusion. With these limitations in mind, each topic begins with a brief overview of the current situation, followed by a summary of insights from our expert interviewees.

4.1. Summary of key insights about purpose, strategy, materiality, disclosure and stakeholder engagement

Key insights into purpose, strategy, materiality and disclosure

There seems to be:

- increasing discussion around purpose at board level, but with some confusion over how it is understood, and limited evidence that it is systematically driving strategy
- an increase in strategic engagement by boards, although starting from a low level, and indications of more integration of sustainability issues and purpose, but the general approach is through information provision and acquisition
- an increase in the use of and discussion about materiality assessments by boards. However, any move towards using 'double' or more 'impact materiality', away from 'single' or just 'financial materiality' is harder to assess. At the moment that shift, and its influence on strategy, appears limited
- some indication that boards are slowly seeing ESG (and integrated) reporting, and the data acquisition underpinning it, as part of overall strategy development, and not just as a compliance requirement.

Key insights into stakeholder engagement

There seems to be:

- a stable and high level of intent by boards to engage with shareholders and wider investors, with indications of an increase in shareholder relations beyond annual general meetings (AGMs). However, there is also evidence of tension emerging between the board and shareholders
- a growing narrative around the benefits and most appropriate ways to engage stakeholders by boards, as well as an increase in stated corporate stakeholder engagement. It appears, however, that practice remains dominated by engagement with financial stakeholders
- slow and emergent signs of increasing innovation in how boards engage with non-financial stakeholders.

4.2. Purpose

There seems to be increasing discussion around purpose at board level, but with some confusion over how it is understood, and limited evidence that it is systematically driving strategy.

The first thematic area to be discussed in Domains 2 and 4 is that of purpose. As we outlined in **Phase 1: Part 1**, discussions about the 'purpose' of a company have been evolving, particularly over the last ten years. Purpose has become a rapidly developing topic of discussion at the highest levels of business and academia, informing the Purpose-driven approach outlined in this report. A more detailed overview of the evolution of the concept, situating it in the broader literature on the topic, can be found in a related CISL publication.[139] For the purposes of this discussion, we have drawn out some of the most notable and recent shifts in the academic debate, particularly those moving away from a BAU position, before

exploring how this shift is appearing in conference agendas, practical toolkits, and emerging codes and standards.

The Future of the Corporation programme is the British Academy's review of the role of business in society, combining research from a range of academic disciplines with insight from senior business and policy leaders.[140] The final report of the programme draws upon four years of research, engagement, polling and collaboration with other initiatives to conclude that there is a growing appetite for purposeful business – defined as a "system in which the purpose of business is creating profitable solutions for problems of people and planet, and not profiting from creating problems". Profitable in this sense does not, however, mean maximising returns, but rather a level which is adequate for reinvestment and rewarding key stakeholders appropriately. It specifies a need, however, to create a more supportive legal, regulatory, governance and reporting framework, in order to deliver both accountability for, and implementation of, purpose. One principle is that of aligning managerial interests with company purpose and establishing accountability to a range of stakeholders through appropriate board structures, as well as determining a set of values necessary to deliver purpose, embedded in the company culture. Specific recommendations include companies placing purpose at the heart of their annual reporting and demonstrating to their stakeholders how their ownership, governance, strategy, values, cultures, engagement, measurement, incentives, financing and resource allocation deliver it.

Eccles et al. (2021) argue that while corporate purpose and sustainability are now part of the mainstream lexicon in the corporate and investment communities and are used interchangeably as synonyms, the two concepts are related but different: "Purpose comes first. Sustainability can either contribute to it or can detract from it … Long-term sustainable value creation starts with clarity of purpose. The products and services that are the solutions for people and planet will need to change as the world evolves in terms of its sustainability concerns about the negative externalities created by these solutions. Addressing these externalities must be done in a way that keeps the solutions profitable. Failure to do so will result in sustainability detracting from purpose, rather than supporting it."[141]

In contrast, more recent work emphasises the inextricable connection between purpose and sustainability.

PAS 808:2022 is a guidance document from the BSI (the UK's official standards body) on *Purpose-driven organisations: Worldviews, principles and behaviours*. The report sets out a definition of Purpose-driven organisations that breaks with conventional thinking and creates (or refocuses) the organisation to meet the goals of sustainability (meeting the needs [or wellbeing] of present and future life on earth) within the required thresholds of healthy systems and resources,[142] including healthy stocks and flows of financial capital. In summary, Purpose-driven organisations:

- exist for a meaningful end – to achieve an optimal strategic contribution to the long-term wellbeing of all people and planet (sustainability)
- make sure that, at a minimum, and regardless of its purpose, they make a fair and adequate contribution to ensuring that the systems, capitals and stakeholders on which they rely are healthy, and
- approach these two tasks with decision-making that is both wise and ethical.

The rise of interest in, and practice towards, Purpose-driven organisations can be seen in its increasing presence on the agenda of global conferences, and is being tracked by various companies and academic institutions.

Recently, some key annual conferences have turned to the particular issue of corporate purpose and stewardship, with a focus on the business's role in wider society and the board's role in making decisions for a sustainable future. For example, the European Corporate Governance Institute annual conference in September 2023 explores Modern Capitalism and Corporate Purpose[143] while the International Corporate Governance Network's latest 2023 annual conference explores the role of governance in "meeting business needs for today and the future … [i]n a time of multiple environmental, social and governance crises"[144] building on two previous years with a central theme of ESG and stewardship.

Russell Reynolds Associates reported a global trend in 2020 around the increasing importance of corporate purpose. The review noted that, while corporate purpose and stakeholder considerations have been business norms in various parts of the world for decades, the 2019 US Business Roundtable amended Statement on the Purpose of a Corporation, followed by a December update to the World Economic Forum 2020 Davos Manifesto, are indications that public opinion in many countries appears to be shifting against shareholder primacy, even as there remains scepticism concerning the practical application of these documents.[145]

A global study conducted by EY for Harvard Business Review Analytic Services[146] assessed the Business Case for Purpose, with responses from North America (42 per cent), Europe/Middle East/Africa (28 per cent), Asia-Pacific (23 per cent) and Latin America (7 per cent). They found that a strong sense of collective purpose drives employee satisfaction (89 per cent), affects an organisation's ability to transform (84 per cent) and helps increase customer loyalty (80 per cent). The survey defined organisational purpose as "an aspirational reason for being which inspires and provides a call to action for an organization and its partners and stakeholders and provides benefit to local and global society."

The rhetoric is also being turned into reality as companies adopt the approach, and consultancies and others develop practical toolkits, or reach greater clarity of the role of the board, to enable companies to become Purpose driven. Additionally, the concept is being incorporated into global standards on governance which place purpose as the primary governance principle.

Strandberg (2023) asks: "What is the role of the board in providing oversight of the company's purpose and stakeholder relationships?". The author draws on 43 publications between 2018 and 2023 including trade publications, media sources, white papers and research. The definition of purpose is anchored in those offered by the British Academy Future of the Corporation programme, ISO 37000, PAS 808, and the United Way Social Purpose Institute, and is summarised as "creating a better world in which that is the reason the business exists". The report concludes with six areas of specific oversight responsibilities, listed as 30 questions for directors to ask, relating to:[147]

- purpose and strategy
- stakeholder engagement

- culture and decisions
- governance protocols
- monitoring and reporting
- knowledge and education.

ISO 37000 is a global standard for the governance of organisations, published in 2021 as a consensus document signed off by 164 countries, with 77 countries involved in its development, and with 25 liaisons, including the UN. In the standard, the first and primary principle concerns purpose, with the governing body ensuring that "the organization's reason for existence is clearly defined as an organizational purpose". This organisational purpose defines the "organization's intentions towards the natural environment, society and the organization's stakeholders", and ensures that "an associated set of organizational values is clearly defined". This purpose principle is understood to be the 'primary consideration' for governance and the "central point" of all the other principles in the standard.[148]

The four foundational governance principles in ISO 37000 – building on the primary principle of purpose, are:

- determining the organisation's approach to value generation
- directing and engaging with strategy to generate that value
- overseeing that the organisation performs and behaves according to the expectations set out by the governing body, and
- demonstrating accountability for the organisation's performance, behaviour, decisions and activities.[149]

Having charted some of the signals that the broader debate around purpose is shifting, with some of these shifts becoming codified in soft governance through voluntary frameworks and standards, accompanied by emerging examples of practice, we now turn to the data we collected around whether these shifts are being felt at the level of generic board practice.

4.2.1. Insights about the board's understanding of purpose

One interviewee articulated the ideal of purpose:

> *"It's … your North star to help you make all the tough decisions as a business. It's the direction in which you're going to go … And if that means selling, or getting rid of some cash cow, so be it. If this means not paying a dividend for three quarters in a row because you're investing into something that you fundamentally believe in, so be it. If it means falling share prices – your board, your investors, you as a manager, as a CEO, you're OK with that? I think for me, that's what a solid purpose is." (26)*

Many of our respondents are well aware of the evolution of this term to talk about a specific Purpose-driven way of doing business – one which is fully aligned with short- and long-term wellbeing and sustainability requirements. Others, however, drawing directly on the dictionary definition and legal term rather than the emerging concept connected with purposefulness, focus their responses on a more

generic use of the term, as the main aim and motivating force of a company, regardless of how it interconnects with the long-term wellbeing of people or nature.

The initial insights of our expert interviewees tend to suggest that purpose is being increasingly recognised as important to both the company and the board.

> *"The importance of purpose is much more universally recognised or much more widely recognised than once it was. It's not just … an adjunct to the marketing department. There is more senior time invested in trying to define purpose as being an important exercise, a useful exercise and an exercise that helps the company know itself to fulfil its mission to serve its stakeholders." (27)*

4.2.2. Insights into the role of the board in relation to purpose

The comments from interviewees reveal a continued lack of clarity on the role of the board versus management with respect to purpose. However, several areas of relative consensus emerged:

- the board being involved in the creation of the purpose, and the realisation of related strategy
- alignment between the board's and the CEO's vision of purpose
- holding the executive to account for the enactment of purpose.

The current global consensus which led to the creation of ISO 37000 puts purpose as the primary responsibility of the board. However, it seems that for some of our interviewees, the prevailing driver of purpose is currently the executive management. Articulating the relative roles of the board and management with respect to purpose is an evolving challenge.

> *"I think the articulation of purpose … should be embedded in the strategy of the company, and that strategy is driven by the top management. It's overseen by the board, or supported by the board in its creation. But fundamentally it's something that CEOs and top leadership do." (26)*

> *"Where I see some of the companies who have done this very, very well, it's been because there has been a strong alignment between the CEO's vision for the purpose of their company, how they're articulating that, and strong alignment with the board … They understand the trade-offs having such a purpose would entail. And then the board is right behind the CEO in support of that strategy, which is the ideal world scenario … The board also provides input on what the purpose should be … I think your role is to make sure that you enable, or have the right checks and balances, to make sure that everything that the company is doing is well aligned with the purpose." (26)*

> *"From my work experience, what I've seen is that if, as the board chair or as the board as a whole, if you're convinced, if you've co-created that purpose together … it's easier to keep your executive team or the CEO, keep them honest about it. If the board is not really convinced, or it's not engaged, or it hasn't played an active role in shaping that purpose, then it becomes very, very easy for all of this to be a 'tick the box exercise' for the board, as well as for your executive leadership team." (26)*

The Enacting Purpose Initiative provides boards and senior executives with a simple framework to govern purpose. The SCORE framework is based on five mechanisms that facilitate the translation of purpose intent into purpose action:

- simplify into a simple and precise statement of purpose

- connect to strategy and capital allocation decisions
- own the purpose and put in place appropriate structures, control systems and processes
- reward through measures of performance that evaluate the success of the organisation in delivering on its purpose
- exemplify through communication and narrative strategies.[150]

Several interviewees mentioned a driver of this increased engagement of boards with purpose, that it was what consumers and other stakeholders expected from a company, and that it was perhaps even becoming a necessity:

> *"I'm optimistic, you know, because increasingly markets are rewarding it, consumers are rewarding it – this kind of authenticity … If you're not authentic, I think the cost is very high. The risk is very high. So either you do it ideally as some kind of a value creation activity or at a minimum you do it because you don't want to eliminate the value that you have been able to create." (26)*

> *"They need to have one (purpose), you need to have in the annual report … and we need to be able to tell people what it is." (2)*

> *"What is our organisation about, and how do we look at it in the context of a very changed world where you have more aware consumers who are looking at how you do things?" (13)*

There was also a suggestion that generational change among company employees, and related pressures on recruitment, was leading to an increasing focus on being more Purpose driven.

> *"The new, the younger generations are really rocking the boat. And it's on the news every day … Current generations of 20 year olds just don't think about work the same way that people of my generation thought about work … They've got to work for a company that has a purpose. So put one of these people into a boardroom and they'll be asking: 'What's our purpose?' So I think it will change and I think it will change … quicker than we think." (21)*

However, there was also a range of challenges. Firstly, many companies and boards are paying lip service to the idea of purpose, but not making it a reality, even if it is shaping strategy.

> *"Without actually enacting or believing in it, purpose is just words on the wall … You hire a marketing firm or communications firm to develop something really crunchy, and that's it. And then you forget about it, and go on with business as usual." (26)*

> *"Sometimes I think that [purpose] gets really stretched because a business that provides a genuine service, and good in the world, can find it quite easy to say what their purpose is. But other businesses, which are reliant on selling vast quantities of a product or a service which doesn't easily fit into that box … you end up with a statement or a strategy which really doesn't have much substance to it. It's just a reframing of sustainability, or a reframing of CSR in another guise." (17)*

> *"So definitely a lot more talk about it. But … it can still get a bit generic, and a bit fluffy, and then it's tick the box." (20)*

The United Way Social Purpose Institute in Canada partnered with Corporate Knights (a media and research company) in 2022 to develop a new rating to assess the degree to which companies with a stated

social purpose are governing, implementing and disclosing progress on their purpose.[151] Within this rating, a purpose business is understood as a business whose "enduring reason for being is to create a better world". The rating criteria were applied to 34 businesses with headquarters or significant operations in Canada – out of an initial sample of 197. These companies met the gateway criteria of having a stated purpose that creates value for society, rather than solely for shareholders or customers.

The report concluded that, even in this small sample that are 'ahead of the pack', there are few companies with clear societal purpose embedded in their purpose statements, and purpose is often conflated with ESG and CSR. Moreover, companies are taking action to embed their social purpose in some areas more than others, for example culture, strategy and disclosing progress, but are lagging in board oversight and the CEO role. Nonetheless, a five-step transition pathway emerged that companies can take on their journey from purpose adoption to implementation:

- embed social purpose in the culture
- disclose social purpose progress
- embed social purpose in the corporate strategy
- embed social purpose in incentive plans and performance objectives
- embed social purpose in board and CEO mandates.

And secondly, the interviewees also suggested that there are few examples of boards that are truly Purpose driven, and that have really taken the hard decisions that arise when working through the implications of the Purpose-driven logic.

> *"I think that we are far from getting them to understand that repurposing needs to look at sustainability beyond profits, and to include engagement of people, their carbon footprint. To include really what the Brundtland Commission spoke to in terms of … ensuring that their resources are available for future generations. I don't think we have got there with boards just yet." (13)*

> *"There are businesses I've worked with who spun off their cash cows simply because it was not aligned to what they wanted to be when they grew. It was not aligned to their purpose. Those are very hard decisions. There's a lot of challenge … very few companies have been able to do it. It's hard." (13)*

A 2020 PwC study[152] within the US found that, while almost 80 per cent of business leaders believe that purpose is central to business success, and to an organisation's existence, 93 per cent failed to state why their company is in business. They concluded that "most purpose statements lack any meaningful sense of purpose". Although 77 per cent of the purpose statements alluded generally to what the organisation does, 95 per cent "neglected to mention a core problem they endeavour to solve or to reference their organization's founding histories in a way that could further illuminate the purpose for which their organization exists or why it was founded". The report also highlighted that more than half of respondents (51 per cent) failed to mention any beneficiaries.

CVS Health, the pharmacy chain, banned the sale of tobacco products in 2014, despite this being a $2 billion revenue stream per year.[153] They felt that selling tobacco did not fit with their purpose, and that

according to their CEO in 2019, "the private sector can have a real impact in addressing the country's greatest social challenges, without having to sacrifice the pursuit of profit."[154]

Our expert interviewees also recognised that there can be a difficulty in finding a purpose which works for all key stakeholders. For example:

> *"Often the stakeholders … there's going to be a conflict between them … Can they come up with a purpose that unites them all? Very difficult … Coming out with a purpose that genuinely your customers, your employees, your shareholders can all get behind? … [The result might therefore end up being:] Let's have a purpose that doesn't offend anybody." (2)*

4.3. Strategy

There seems to be an increase in strategic engagement by boards, although starting from a low level, and indications of more integration of sustainability issues and purpose.

The second thematic area to be discussed emerging from Domains 2 and 4 is around strategy. Whether or not a board is adopting a Purpose-driven approach to strategy creation and/or oversight, it is useful to first understand current trends in how boards are engaging with strategy per se, and the extent to which they are incorporating ESG and sustainability issues.

4.3.1. Insights into boards' engagement with strategy

'Strategy' and 'strategy formation', were mentioned by over a third of interviewees. Overall, interviewees felt that there was an increasing move towards more engagement by the board with strategic decision-making.

> *"Strategy is being much more focused upon by boards. They're spending more time on strategy, and I'm seeing that particularly in terms of strategy retreats … typically now one or two days … [with] management and the board members. And when I do board evaluations, without any doubt, what all of the directors will say, and all of the management will say: 'We should spend more of our time on strategy'." (22)*

However, this trend seems to be starting from a low level. Most companies seem to be relatively hands-off, approving strategy that has been created by executive management without ensuring the strategy has been thoroughly vetted.

> *"In most of the cases that I see … except for a handful of companies that are really sophisticated … I see a lot of companies that simply sign off on a strategy that comes from management, and without a lot of time dedicated to think the strategy through." (23)*

One suggested implication of this greater attention to strategy, because of the limited time available for board decision-making (Section 3.3), was that it reflected a move away from governance as just being about compliance, with the traditional functions of oversight and control becoming, or having already become, less dominant. As one interviewee said, it may be more about:

> *"…how to prepare for the future, and less on oversight and control." (8)*

However, while a more strategic focus may be recognised as an ambition by boards, other respondents noted that strategy in general may still be pushed off the board agenda by a traditional focus on financial compliance:

> *"We start with the financials and then … at the end … OK, anything else and then people start talking about strategy" but "I think we are getting to the point where we're talking more about strategy up front than at the end, where everyone is too tired." (11)*

There are also indications of geographical differences in strategic approach, an area in need of further exploration.

> *"Emerging markets are not exactly on trend with this topic … I've seen most of the boards that I see and interact [with], look at the past and not so much of the future." (23)*

4.3.2. Insights into boards' incorporation of ESG and sustainability issues into strategy

There was some indication from our expert interviewees that sustainability issues and ESG factors were becoming a greater part of strategy creation or oversight for some boards, although this practice was not widespread.

> *"We're seeing lots of big decisions being made and based on climate risk or ESG risk, but that's not necessarily cascading up into big … strategic transformation decisions." (15)*

The BCG–INSEAD Board ESG Pulse Check survey in 2022 – which surveys 122 board directors across a range of sectors and geographies (albeit with a majority from Europe) – found that, while 91 per cent of respondents think their boards should devote more time to strategic reflection (rather than operational management) on ESG issues, more than half (53 per cent) said they are not effective in doing that, and 71 per cent reported that they are only moderately, or not at all, effective at integrating ESG into company strategy and governance.[155]

PwC's 2022 Annual Corporate Directors Survey, based on 704 public company directors in the United States, reports that almost two-thirds of directors (65 per cent) say that ESG is part of the board's enterprise risk management (ERM) discussions, and an increasing percentage of directors (55 per cent, up three percent from last year) say ESG is regularly a part of the board's agenda. At the same time, only 57 per cent of directors say ESG issues are linked to company strategy, down from 64 per cent last year, while only 45 per cent of directors think that ESG issues have an impact on company performance, down nine percent from a year ago. It is worth noting that a range of topics are included within the umbrella of 'ESG', with data security and talent management getting much more consideration (over 90 per cent of respondents reporting coverage in the last year) than human rights issues and corporate political activity (less than a third).

The survey also reports that company size has a significant impact on potential ESG integration. Large company boards are more than twice as likely to have discussed climate change, carbon emissions and the company's stance on social issues, while the directors of large companies are more likely to say that the board understands the company's ESG risks, ESG opportunities, climate risk/strategy and carbon

emissions, and are more likely to say that ESG is linked to the company's strategy and is a regular part of the board agenda.[156]

A suggestion from one interviewee of why boards are engaging more strategically and particularly including ESG and sustainability, in addition to that of greater awareness of external pressures, was the impact of COVID.

> *"I think that urgency has really accelerated now … if you bring up something that needs board oversight and board direction or strategy change, I think there's much more cognisance that … it should be on the board agenda than there was three years ago … it's no longer a nice to have, or do our best. We'll fit it in." (15)*

4.3.3. Insights into the inclusion of purpose in strategy by companies and boards

Discussions and statements by companies and boards have not, according to some interviewees, always moved beyond 'statements of intent' of purpose to using purpose to drive strategic decisions.

HBR's study[157] concluded that only 46 per cent of corporate executives used purpose to inform their strategic and operational decisions, even though 90 per cent believed their company understands the importance of purpose.

Using PAS 808:2022 as the benchmark for 'best practice' on purpose, Blurred (a global strategic and creative consultancy) has launched a methodology and tool for measuring the effectiveness (or otherwise) of a company seeking to integrate ESG and Purpose (ESGP) as a strategy for positive impact.[158] Using tens of thousands of ESG and Purpose disclosures (annual reports, ESG reports, integrated reports etc) across the FTSE100 dataset to identify trends, the research revealed an apparent correlation between the volume of ESG disclosures and how much companies talk about purpose. Analysis of each business's stated purpose against the PAS 808 standard led the consultants to conclude that no companies fully aligned with best practice, but with 42 per cent on a spectrum towards best practice. While the methodology focuses on stated purpose, and not the substance and actions behind that statement, the findings have informed three core criteria for effective integration: ESGP integration across core narrative; evidenced in values and behaviours; and maintained with clearly communicated governance.

Boards also seem to be finding it hard strategically to manage today's customer needs alongside future needs which are more closely aligned with sustainability and wellbeing, in other words, to effect transition:

> *"In different industries and in different geographies … they need to make decisions today to be relevant tomorrow. But how do we develop something for which the demand is not that great yet? … We need to operate in today's world for tomorrow and be ready for tomorrow. But when do we switch? How do we develop these two things at the same time? I think that is a crucial topic." (18)*

4.4. Materiality

There is an increase in the use of and discussion about materiality assessments by boards. However, any move towards using 'double' or more 'impact materiality', away from 'single' or just 'financial materiality' is harder to assess. At the moment that shift, and its influence on strategy, appears limited.

The third thematic area to be discussed emerging from Domains 2 and 4 is around materiality. One of the main factors that impacts on how a board understands and creates its strategic direction is that of understanding what is material to strategic decision-making. Materiality can be understood in different ways, a situation which seems, according to our expert interviewees, to have created confusion within boards, or even not be seen as an area in which they should be concerned.

Materiality was raised as a topic by a third of the expert interviewees, reflecting the increase in discussion about this concept globally.

4.4.1. Insights into how boards understand, and use, the concept of materiality

The different conceptualisations of materiality were covered in Phase 1: Part 1 and how they relate to the different organisational logics, in Background to the study and research framework, at the beginning of this report. While there are many materiality terms, the most commonly used ones are summarised in Table 26.

Table 26: Different types of materiality

Type of materiality	Scope[159]
Financial	Issues which, above a certain threshold, could impact on the decisions made by the users of that information, and on subsequent financial performance and reported profits.
Single	Aspects of the external environment that can significantly affect a company's business model or profit.
Double	The impact of the business on the environment, stakeholders, wider society and the economy (impact materiality); *as well as* their impact on the company itself. This concept is currently contested in its understanding of impact on the world, whether financially relevant or not to the company.[160]

There seems to be increasing attention by companies to materiality. Datamaran assessed mention of terms such as 'materiality matrix', 'materiality analysis', 'materiality assessment', 'issues prioritisation', 'double materiality' and 'dynamic materiality' in 2020. They found that mentions rose from 202 in 2011 to 1,695 in 2019 out of their database of 8,000 global companies.[161]

Board members seem to be very unclear on their role with regard to materiality, and how to understand it. Comments included:

> *"There's still a lot of doubt and questions in the market … What do I have to report? What's material? What's not material?" (23)*

> *"There [are] some people who very firmly believe, [they] should look at the financials and that's [their] role as stewards, whereas other people do see a broader role." (20)*

There does, however, appear, from the comments made by interviewees, to be a trend in relation to the increased use of materiality assessments. However, there seemed to be little evidence that these materiality analyses are currently being systematically incorporated into strategy.

Materiality assessments are systematic processes to identify and prioritise ESG and sustainability issues that a company might be affected by, either directly or indirectly via the company's effect on those issues.[162]

It seems from the interviews with our experts that board members are generally responding to regulatory and legislative requirements – in other words compliance – and trying to work out the easiest way to proceed.

One interviewee said:

> *"I think when it comes to materiality it's happening for the simple reason that suddenly I need to sign off on some of this disclosure." (11)*

A sustainability consultant from the Netherlands emphasised this reactive approach:

> *"There tends to be this … tick box mindset [from point A to point B]. We've got this ESG thing we need to do. There's a bunch of data. Here's the materiality assessment. OK … we [now] need to do double materiality … [therefore we need] a set of stakeholders. That's point B. What's the most direct route?" (20)*

Some of the available statistics help us to identify the kinds of approaches to materiality being used, and show that companies range from not measuring, to using single, double and impact materiality.

A 2022 survey by Corporate Board Member and Diligent Institute, What Directors Think, found that of 400 directors from US public companies who participated in the study, 78 per cent conducted materiality assessments. Almost half (49 per cent) reviewed their materiality issues every 3–6 months, with 29 per cent on an annual basis.[163]

PwC found in their Annual Corporate Directors Survey in 2022 that only 11 per cent of boards they surveyed understood material ESG risks.[164]

The consulting firm KPMG produced a global Survey of Sustainability Reporting in 2022 (one of the most comprehensive non-academic studies looking at disclosure practices), which included a new question

specifically on materiality assessment and reporting.[165] They analysed financial reports, sustainability and ESG reports, and the websites of 5,800 companies in 58 countries, territories and jurisdictions. The companies surveyed include the G250 (the world's 250 largest companies by revenue, based on 2021 Fortune 500 rankings) and the N100 (a worldwide sample of the top 100 companies by revenue in 58 countries, territories and jurisdictions). They found that around three-quarters of companies perform materiality/sustainability assessments – 71 per cent (N100) and 77 per cent (G250).

KPMG also broke down the analysis into different kinds of materiality assessment used by companies. The criteria used are specific for the G250 as:

- 8 per cent – 'impact on the company' – single materiality
- 39 per cent – 'impact on the company and its stakeholders' – double materiality
- 30 per cent – 'impact on the company, its stakeholders and broader society' – impact materiality
- 23 per cent – did not measure materiality.

A stakeholder engagement consultant felt that some of this difference in understanding of different kinds of materiality was related to generational differences:

> *"I'd say probably more the older generations, there's quite a linear way of thinking … what's immediately in front of us in the next 2–3, five years, how's it potentially going to impact the organisation and executive management?" (20)*

Another key challenge raised was that different ideas of materiality are operating within different companies and across geographies, particularly around:

> *"…single and double materiality … [which is] still quite divided." (20)*

> *"I think it's well known now that in the EU it's the double materiality and in the US it is the single materiality" (18)*

4.5. Reporting and disclosure

There seems to be increasing involvement by the board in overseeing ESG and sustainability reporting and disclosure (including integrated reporting).

There is some indication that boards are slowly seeing ESG (and integrated) reporting, and the data acquisition underpinning it, as part of overall strategy development, and not just as a compliance requirement.

The fourth thematic area to be discussed emerging from Domains 2 and 4 is around reporting and disclosure. A key aspect of a company's performance, whatever logic it is adopting, is that of identifying and reporting on actual outcomes of business performance and impact, as well as being transparent over these results. This section is inextricably linked with the three preceding sections on Purpose (Section 4.2), Strategy (Section 4.3) and Materiality (Section 4.4), all of which help determine what is reported on and why.

As we saw in Phase 1: Part 2, reporting and disclosure practice and requirements are evolving from a historically predominant focus on financial income and sound governance of financial stocks and flows, to one which includes a greater range of non-financial capital accounting, ESG metrics and disclosures. This evolution comes with related enhanced levels of accountability with regard to a company's adherence to legal and regulatory requirements, accepted norms of appropriate behaviour, as well as shareholder and other stakeholder pressure.

A 2022 survey of 400 directors of US public company board members, *What Directors Think*, by Corporate Board Member, Diligent Institute, found that 75 per cent believed that ESG continued to rise in importance for them, and that their company is now reporting and disclosing ESG goals and progress at least annually.[166]

Alongside the pressure of mandatory legislation and regulation, as well as voluntary standards, codes and international frameworks, other reinforcing drivers include the evidence of business benefits from wider sustainability reporting beyond compliance.

A series of global interviews with boards by WTW (formerly Willis Towers Watson) in 2020 found that there were positive benefits of reporting on consumer retention and recruitment (72 per cent), cost savings (71 per cent), insurance/credit agency engagement (71 per cent) and reduction in long-term risk (71 per cent). The majority of respondents also noted that ESG reporting has improved employee morale (71 per cent), employee recruitment efforts (69 per cent) as well as investor and stakeholder relationships.[167]

There is also pressure from stakeholder and shareholder activism.

Larry Fink, for example, Chairman and Chief Executive of BlackRock, in his 2022 Letter to CEOs, believed that shareholder activism is particularly adding pressure to companies and their boards to better account for their activities, provide assurances that they are effectively managing material interests and risks, and that they are accurately reporting (both successes and shortcomings) their performance as it relates to their strategy.[168]

However, although the general direction of wider company reporting and disclosure practices is being informed, encouraged and required by developing standards, legislation, regulation and good practice, it is unclear how this changing landscape is affecting the role and activities of different company boards around the world. We also know very little about the relationship and responsibilities between the board and executive management with regard to this topic, or the extent to which reporting and disclosure, does or does not link with board-level strategic decision-making.

4.5.1. Insights into board understanding and use of non-financial reporting

Some of our interviewees made the point that most boards are comfortable with financial reporting, finding it "relatively straightforward" compared with ESG and sustainability reporting. Interviewees felt that ESG data, as well as ESG risks, could be difficult for board members to understand and manage, since it had:

> *"some of that complexity … which is quite different to financial data." (20)*

In the 2020 What Directors Think survey for the US, respondents expressed "plain frustration with yet another item being tacked onto the board's agenda", not just because this implied additional work and accountability requirements, but more because there were concerns about their ability to understand sustainability issues enough to have effective oversight and govern appropriately.

This need for greater skill and knowledge around ESG and sustainability more widely, in order to take on responsibility for overseeing ESG and integrated reporting effectively, is explored further in Section 4.5.

Several interviewees thought that there were slow moves by boards away from seeing ESG and wider sustainability reporting as just something that had to be complied with (and hence a 'tick-box' exercise) to recognising the wider implications for the organisation of using sustainability information to inform the realisation of purpose, and strategy creation, or to use them as part of the targets around which the success of the company, and individual employees, including the CEO, can be assessed.

> *"There's the very immediate – What we're going to do on net zero? How are we going to get there? What are we going to publish this week or next year? And then there's the much more long term: what does this really mean for our organization, for the team in terms of the types of people, what education do we need, what training do we need? I sense a shift more into that, but I think it's still slow moving from that compliance mindset more into that really true looking forward mindset." (18)*

As a result of this increased ESG and sustainability reporting, one interviewee made an interesting comment that there may need to be better ESG control systems, similar to financial control systems. The implication of bringing these two systems together would be more:

> *"…'integrated governance' … because … the compliance function and the risk management function and the audit function are all … controls in the system. So in additional financial controls, I need other controls now. All of this is now making the oversight function and the system through which I do that … more sophisticated and more strong."* (18)

4.5.2. Insights into challenges for reporting and disclosure

One difficulty with these trends towards the increasing scope of reporting and disclosure, raised by several interviewees, is that there is an excessive focus on compliance due to the extent of the requirements, and concern that too much reporting compliance can push out strategy and innovation. However, it has to be noted that often in practice, regulation can lead to positive innovation.

> *"Clients are so preoccupied with the concept of disclosure as a compliance tool and a compliance objective. That's dangerous for a number of reasons. One of the reasons is that they allow it to drive their business strategy … What they should be doing is defining their business strategy first, and then the way in which that's implemented should drive their disclosure. By putting the cart before the horse this is a damaging trend because it actually means that the quality of the disclosure is poor. But it also means that the strategy that is developed is often inauthentic, and you end up with something which is little more than window dressing." (29)*

> *"Actually, regulation is really a constraint. It's on the To Do list. It's something they've got to get through and tick off and make sure that looks credible and it doesn't look like green washing. It's sort of constrains them innovating and looking at how to get collective advantage and competitive advantage." (15)*

Some concern was also expressed about how these perceived excessive compliance requirements may lead to board decisions to either remain, or become, private. This uneven playing field between listed and unlisted has resulted from the focus of legislators on the former market, since it tends to represent the largest companies.

> *"Regulators did pick the lowest hanging fruit. They started with the senior market listed companies on a number of stock markets throughout the world and then the junior markets. This is important because that evolution is within one system. All of these companies have a publicly traded stock of some sort." (29)*

Interviewees had also heard calls for more legal and regulatory standardisation from board members due to the differences in reporting and disclosure requirements of different jurisdictions.

> *"They feel it is not an even playing field." (18)*

According to a report by Spencer Stuart, a global executive search and leadership consultancy, directors are particularly concerned about the lack of standardised reporting.[169]

However, one interviewee felt we were in *"a phase of consolidation and standardisation",* and that the next stage of development will become an *"auditing phase" (18).*

The danger of greenwashing was mentioned many times by interviewees, and suggested by one interviewee to be partly related to the lack of clear quality controls and oversight by boards and management on the accuracy, completeness and robustness of ESG data.

Interviewees noted widespread disagreement between companies about where the ESG reporting and disclosure function should sit within the organisational structure, for example, should it be with the chief financial officer, the CEO, the legal officer or the compliance officer?

Within the US, the What Directors Think survey found that different parts of an organisation dealt with sustainability reporting, with a third saying it was led by the Chief Sustainability Office (CSO) (35 per cent), operations and facilities (35 per cent), finance (30 per cent) and human resources (28 per cent), with other departments seen as playing an important role in reporting being investor relations, marketing and communications, procurement and legal/compliance.

It was also noticed across some secondary literature that the nature of the reports produced seems to be one-sided, in other words, from companies to stakeholders, and with limited opportunity for feedback from stakeholders. This lack of engagement could therefore reduce the effectiveness and development of strategy and decision-making, and increase the likelihood of greenwashing.[170]

4.6. Stakeholder engagement

The fifth and final thematic area to be addressed from Domains 2 and 4 is around stakeholder engagement. There has been a great deal of theory, and evidenced practice, about how the stakeholders of a company are important to business success, as well as some more limited evidence supporting the achievement of positive sustainability outcomes through their engagement with a company.[171,172]

The evolving discussions and practice around Purpose-driven companies puts a stronger emphasis on the contribution of appropriate stakeholders to strategic decision-making itself, as well as a more nuanced

view of different kinds of stakeholders, and their relation to the company. Shareholders are stakeholders like any other under this logic, fundamentally challenging the shareholder primacy model.

Nearly all expert interviewees mentioned that stakeholder engagement by boards, including and beyond shareholders, is important, but that slow progress is being made.

The Global Trends Survey indicated mixed responses about the pace of change for stakeholder engagement. Of the 12 areas covered in the survey, stakeholder engagement was ranked 7th fastest changing, so not a leading area. There was also some indication of age differences, with younger respondents perceiving it as a slower, or less obvious trend, than older.

What is a stakeholder?

The international governance standard ISO 37000 defines a stakeholder as a "person or organisation that can affect, be affected by, or perceive itself to be affected by a decision or activity".[173] This definition therefore includes shareholders and investors, employees and customers, regulators, as well as the community, or suppliers. It also includes civil society (such as NGOs), the wider public, and future generations.

The inclusion of the environment as a stakeholder is controversial, and was not included in the ISO 37000 definition after much debate to align with legacy consensus. However, it has been seen as a stakeholder in other contexts, such as by the World Economic Forum,[174] and has become part of governance processes, for example by being proxied on unitary boards and compound boards (companies with multiple boards).

The 2022 BSI PAS 808, *Purpose-driven organisations: Worldviews, principles and behaviours*[175] creates a classification of stakeholders which fits with this approach and which is based on the nature of the relationship with the organisation:

a) **Ultimate beneficiary stakeholders** (all people and planet over the longer term, including future generations as the primary decision-making anchor)

b) **Primary beneficiary stakeholders** (those whose wellbeing the purpose primarily serves)

c) **Influential stakeholders** (those the governing body is legally bound to)

d) **Enabling stakeholders** (those who the organisation relies on to achieve the purpose in the way intended)

e) **Affected stakeholders** (those who are affected by the decisions the organisation makes).

The approach to stakeholder engagement adopted by Purpose-driven organisations goes beyond their contribution to short- or long-term financial value maximisation, the prevailing theoretical approach adopted to date.

Stakeholder engagement has been part of the wider discussion of stakeholder governance, which was popularised in the management literature by R. Edward Freeman's 1984 foundational book *Strategic Management: A Stakeholder Approach*.[176] Stakeholder governance is the broad set of principles that guide how organisations manage their relationships with those actors who affect the organisation, or are affected by it. A stakeholder approach to management relies on a deep understanding of the bargains involved in securing 'stakeholder legitimacy' as a precondition for sustainable corporate performance.

Research on stakeholder governance has highlighted a significant link between stakeholder engagement and enhanced financial performance, since it empowers organisations to gain a competitive edge by cultivating their intangible assets in the form of enduring, robust relationships.[177] Studies also show that the goodwill accumulated by being responsive to stakeholder claims can have an 'insurance effect' on firm value.[178] However, scholars also point to the disconnect between the increasing stakeholder rhetoric of managerial leaders, and actual corporate decision and conduct.[179]

There seems, however, from a survey of the available literature conducted for this research, to be very little insight into how boards engage with different stakeholders (or not), the rationales for doing so, and the role of the board vis-à-vis management with regard to stakeholder engagement.

For this section we have therefore drawn initially from the secondary data that is available and supported this with comments from our interviewees, and some Refinitiv Eikon data where this is relevant.

This limited research is surprising given the rise of interest in, and promotion of, 'stakeholder capitalism' as outlined in **Phase 1: Part 1**.[180] What research there is, however, indicates an increase in board interest, with a particular increase noted during and following COVID-19.[181]

The following sections cover three themes which emerge from our interviews. These are:

- a particular focus on shareholders and wider investors (Section 4.6.1) – both in relation to their impact on the evolving strategic orientation and sustainability impacts of businesses
- practice and discussion relating to stakeholder engagement more widely (Section 4.6.2)
- indications of emerging innovations to improve stakeholder engagement – whether in practice or through governance and board structures (Section 4.6.4).

4.6.1. Insights into board engagement with shareholders

There seems to be a stable and high level of intent by boards to engage with shareholders and wider investors, with indications of an increase in shareholder relations beyond AGMs. However, there is also evidence of tension emerging between shareholders and financial stakeholders.

Responses from our expert interviews suggest that there has been an increase in board-level engagement with investor shareholders over recent years, as well as with investors who are not shareholders.

> *"I think boards have become better at purposefully engaging with investors … I think they are more conscious of their general context, but I think that general context is then managed or engaged more through management and others. So, it's more a delegated engagement." (18)*

> *"Investors have become far more vocal about ESG and the value of it. And certain funds, as you know, will only invest if they feel that a company meets certain benchmarks." (28)*

A 2018 survey by the World Business Council for Sustainable Development found that, in the last few years preceding that survey, there had been a shift from just engaging with shareholders at AGMs, or on 'earnings calls', to more active engagement.[182] A 2022 survey of internal stakeholders at US listed companies and shareholder engagement disclosures at Russell 3000 and S&P 500 also reported that engagement is increasing, especially for medium-sized firms.[183]

In 2022, 60 per cent of directors surveyed by PwC (a 50 per cent increase compared with five years previously) indicated that a member of their board (other than the CEO) had direct engagement with shareholders.[184] Another study examined the extent to which investors initiated engagement with the board. Board directors have experienced a steady stream of activist engagement over the past five years.[185]

This engagement takes different forms and can have a range of outcomes.

Matteo Gatti and colleagues explore some key engagement topics in their chapter in a forthcoming book.[186] These include executive compensation plans, ESG performance metrics, climate targets, energy use reduction, diversity policies, pay equity, and political expenditures. They also show that board–shareholder interactions can have significant outcomes, resulting in board appointments, shifts in company practices, withdrawal of shareholder resolutions and alterations in previously announced proxy votes.

This increased activity has led to some guidelines to support it.

As boards' responsiveness to external stakeholders, including shareholders and investors, comes under scrutiny, regulatory bodies in some countries have also issued guidance on shareholder engagement.[187] In Europe, the EU has been a key regulatory player encouraging shareholder engagement. The EU Shareholder Rights Directive II imposes shareholder engagement disclosure requirements on asset managers and asset owners, recognising that "effective and sustainable shareholder engagement is one of the cornerstones of the corporate governance model of listed companies".[188]

Recent research has also linked shareholder engagement to a broader trend towards the expansion of boards' oversight duties, and strengthened shareholder rights across jurisdictions.[189]

There also appears to be increasing formalisation of the investor relations function within listed companies as a strategic enabler for better corporate governance and market confidence.[190] Researchers have shown that companies that are located in countries that have weaker investor protections, lower disclosure standards and higher global media exposure tend to have enhanced outreach through investor relations activities.[191]

> *"I think the Investor Relations (IR) teams in organisations often have a key role here too … particularly with the shareholder and fixed income holder stakeholder group … What questions are coming up? What questions may be asked or required from ESG ratings agencies, for example? And the IR team … collect that data, summarise it and often present it to the board once a year." (20)*

Although corporate strategy, and its execution, remain key drivers of corporate performance, the investor relations function is increasingly seen as a trust-building tool that supports the management of investor expectations, especially in times of crisis and volatility.[192] A KPMG India survey on the role that investor relations plays within corporate governance architecture indicated that its strengthened position is a result of trying to improve shareholder engagement, boosting the credibility of corporate disclosures, and ensuring compliance with mounting regulatory requirements.[193]

4.6.1.1. Refinitiv Eikon data on shareholder engagement

The Refinitiv Eikon Global Companies Database indicates that globally the percentage of companies that provide information on how they engage with shareholders, and involve shareholders in decision-making, has been at a fairly stable and high level of around 80 per cent since 2017.

The specific wording used by Refinitiv Eikon to capture the extent of companies having what they summarise as a 'Policy for shareholder engagement' is:

Does the company:

- have a policy to facilitate shareholder engagement, resolutions or proposals? (In scope, is the data on [the] company facilitating shareholders to have the right to ask a question to the board or management?)
- allow shareholders to table resolutions or shareholder proposals at the shareholder meetings?

Table 27: Percentage of board policy or practices to support shareholder engagement

	2017	2018	2019	2020	2021	2022
% policy and practice on shareholder engagement	79	79	81	81	82	(78)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

A key problem with this data is that it does not specify if it is the senior management or board members who are responsible for creating and supporting this engagement. There is also a possible bias towards data which reflects engagement at AGMs, rather than ongoing dialogue.

The data varies across geography, with the lowest level in Africa at 52 per cent and the highest in the UK at 93 per cent.

Table 28: Geographical breakdown of 2021 support for shareholder engagement

Geography	Percentage of companies
Africa	52
Asia	81
Europe	72
Latin America and the Caribbean	47
Northern America	92
Oceania	89
UK	93

Across sectors, there did not seem to be much variation.

Much of this increase in shareholder engagement is likely to come from the rise of corporate governance and stewardship codes across jurisdictions (see Phase 1: Part 2), as well as legislation such as Sarbanes-Oxley in the US, which sets out or requires good practice in shareholder relations.

Stewardship codes increasingly recommend that investors adopt shareholder engagement policies and set up robust mechanisms for investor dialogue. For instance, the Hong Kong Principles of Responsible

Ownership state that "where an investor decides not to have a policy on shareholder engagement, they cannot be said to have adopted the principles".[194] The proposed engagement mechanisms include: direct private communication; public strategies such as media campaigns and shareholder proposals; exercising the right to speak and vote at general meetings; divestment; and, in some cases, litigation. In Singapore, the 2022 Stewardship Principles for Responsible Investors also require investors to "describe the progress made and outcomes achieved in shareholder engagements".[195] In the UK, signatories to the Stewardship Code are called to explain how they select and prioritise engagement with investee companies, what are their engagement objectives, the methods of engagement, as well as any engagement escalation processes.[196]

Matteo Tonello (The Conference Board, Inc) and Matteo Gatti (Rutgers Law School) reported in 2019 in the Harvard Law School Forum on Corporate Governance that this legal pressure, along with a rise in shareholder activism towards the company, has encouraged more engagement by companies and boards with shareholders (and other investors) as well as encouraging shareholders themselves to engage more actively with companies.[197]

As the exercise of shareholder governance rights is frequently outsourced to proxy advisors, board members increasingly interact with third-party corporate governance specialists rather than directly with fund managers, adding a layer of intermediation to shareholder engagement activities. Proxy advisors, who provide advice and recommendations about voting to shareholders, are also therefore a key driver of this trend.

Surveys of both directors and institutional investors suggest that proxy advisors are not only information intermediaries but also active standard-setters on shareholder engagement and investor interactions due to their role in informing shareholders' voting decisions.[198]

A field study by Christie Hayne and Marshall Vance in 2019 found that proxy advisors' voting guidelines often define clear expectations of board responsiveness, and condition their voting recommendations on explicit shareholder engagement requirements, which boards must consider to secure support.[199] Although proxy advisors have no legal authority to enforce shareholder engagement, recent research shows that proxy advisors' enhanced monitoring practices, and review of boards' engagement activities, boosts shareholder engagement.[200]

4.6.1.2. Tension between board members and shareholders

There seem to be emerging tensions between board members and shareholders, particularly institutional investors.

Investor groups have taken centre stage in board-level stakeholder engagement. However, the quality of relationships between institutional shareholders and boards is increasingly being put into question. International surveys of business leaders and institutional investors point to a growing disconnect between institutional investors' demands and business practices. Fund managers and senior corporate leaders operate with different priorities and expectations regarding sustainability performance.

In the UK, a recent report on boards' engagement with shareholders at FTSE100 companies revealed that the relationship between boards and institutional shareholders has become strained in recent years.[201] The 2022 *State of Stewardship* report published by Tulchan Communications captured the uneasiness among boards of directors, arising from the increasingly prescriptive expectations of institutional investors, which have been amplified by ever more stringent regulatory requirements. Critics argue that investor stewardship mandates impinge on the responsibilities of boards and divert their attention from strategic business matters to an excessive amount of compliance-focused corporate reporting.

A 2022 EY survey of 1,040 senior finance leaders and 320 institutional investors from over 20 countries reported that 78 per cent of investors would prefer companies to improve their ESG performance even at the expense of short-term profits, but only 55 per cent of companies believe they should do so.[202] Furthermore, 73 per cent of investors consider that businesses have largely failed to enhance their corporate reporting to help investors in their decision-making on ESG criteria.

Institutional investors are stressing the conflict between the increasing governance responsibilities placed on institutional shareholders and the shrinking resources available for carrying out meaningful stewardship activities. The adversarial interactions between boards and investors have led to proposals for the creation of a settlement platform to reappraise board–shareholder engagement.[203]

Institutional investors have also become increasingly frustrated by the growing gap between disclosure based on regulatory tick-boxing along with the release of public statements on the one hand, and authentic and meaningful engagement revealing the hidden story on the other. Formal mechanisms for the board to engage with shareholders can create a way to build trust and mutual exchange that is important for the strategic steering of companies towards long-term performance and sound risk management. In this way shareholders feel that their voice is directly heard by boards rather than being intermediated by investor relations departments.[204] The implication is that stakeholders would rather have direct engagement with the board.

4.6.2. Insights into board engagement with wider stakeholders beyond shareholders

There seems to be a growing narrative around the benefits and most appropriate ways to engage stakeholders by boards, as well as an increase in stated corporate stakeholder engagement. It appears, however, that practice remains dominated by engagement with financial stakeholders.

The recognition and engagement of stakeholders by companies and boards, beyond shareholders, is being mandated or encouraged through new regulation, and codes of governance or stewardship practice around the world as outlined in Phase 1: Part 2. It is also being enabled by a wider interpretation and embedding of a company's fiduciary duty beyond the financial best interest of shareholders. Additionally, there are other more indirect policy levers such as those encouraging asset managers to actively engage in stewardship.

Some corporate governance codes (for example, in Japan) actively encourage boards to appropriately and directly co-operate with stakeholders. Additionally, boards are encouraged to take a leadership role in

establishing a corporate culture where stakeholder rights and interests are respected. However, these codes do not advise on or require specific mechanisms of stakeholder engagement.

Other countries have devised more detailed principles and benchmarks of engagement. Corporate Governance Codes in some jurisdictions (for example, Australia, Hong Kong, the UK) recommend their boards set up investor relations programmes and disclose stakeholder engagement strategies.

South Africa's Corporate Governance Code (King IV Report) requires boards to oversee stakeholder relationship management resulting in methodologies for mapping stakeholder groups and their material interests; formal mechanisms of stakeholder engagement; and measurable indicators of the quality of stakeholder engagement.

In some jurisdictions (for example, China and South Africa), corporate governance codes also require companies to set up stakeholder channels and dispute resolution mechanisms for redressing the infringement of stakeholder rights (links to these codes can be found in **Phase 1: Part 2**.

Other drivers include the level of international rhetoric around 'stakeholder capitalism' by prominent international bodies such as the World Economic Forum, as well as the creation of international principles and guidelines to better incorporate stakeholders within governance. There is also an increasing focus in public policy on supply chain interactions, which is also likely to require business to engage with different stakeholders.[205]

The World Economic Forum used the aftermath of COVID-19 to argue that: "Corporate boards are critical starting points for implementing stakeholder capitalism", and to encourage renewed pressure on companies to consider stakeholders, and provided practical tools to help implement stakeholder capitalism (including having a clear purpose, using ESG metrics and increasing their board diversity).[206]

The British Academy in their work on the Future of the Corporation urges that companies "establish accountability to a range of stakeholders through appropriate board structures" (Principle 4).[207]

In terms of guidelines for engagement, there have been attempts to encourage a more systematic approach to stakeholder engagement by boards, such as by the World Business Council for Sustainable Development. They recommend that boards:[208]

1. Know their stakeholders
2. Understand the expectations of and impact on key stakeholders
3. Ensure key stakeholders are consulted in decision-making
4. Establish governance mechanisms to formalise operational relationships with stakeholders
5. Embed stakeholder discussions into the board agenda
6. Trust the views of stakeholders
7. Act in the long-term interest of the company
8. Acknowledge existing tools and resources that can further embed sustainability

In their Climate Change Boardroom Kit, Chapter Zero recommends that an organisation's leadership should be in tune with stakeholder sentiment and share methodologies for approaches that involve trying to influence other players. They suggest this can be achieved by actively listening to key stakeholder groups through effective communication and engagement, and using transparent disclosure methods to convey strategic decisions. This approach is also seen as being particularly important for investors.

The general feeling among our interviewees was that there was a slow increase in engagement with wider stakeholders.

> *"It's happening more frequently, but it's still not a standard process." (20)*

The majority of boards, however:

> *"…are only starting to think about how are they going to put this in practice in the future"*

and appear to still hold quite rigid views beyond shareholder engagement:

> *"I haven't noticed anything particular yet … It doesn't feel as if this is an issue yet that has landed with boards … all the ones I'm aware of are not yet in a systematic way of thinking about what stakeholder engagement means in terms of their responsibilities." (7)*

The main focus seems to be primarily on financial stakeholders (generally shareholders and investors) as outlined in the previous section. This was referred to as a "*hierarchy in stakeholders"* by one interviewee.

Where wider stakeholder information was deemed useful to decision-making, stakeholder engagement was seen rather to be the remit of executive management.

A World Business Council for Sustainable Development 2021 survey found that it was typically only operational teams or senior management who engaged with wider stakeholder groups beyond the financial.[209]

Interviewees felt that there was a clear sense of unease among board members and a lack of knowledge about how to positively engage with stakeholders, other than shareholders or other finance providers. There may well be a difference here in responses from board members operating on unitary or, for example, on two-tier boards including a supervisory board. In the latter situation stakeholders are often a core part of the supervisory board itself. As a stakeholder engagement consultant said about their colleagues:

> *"We leave it to management to maintain relationships with other stakeholders. When it comes to boards actively engaging with stakeholders through like a stakeholder council, or some mechanism, it was less clear that boards felt comfortable … and knew what to do with that kind of level of engagement. So, there was a … reluctance to … do these staged events … as part of our board duties, we do these country visits, we'll meet some stakeholders, we'll do some handshaking. But you know, this could become a real distraction. There were very few directors that actually understood the kind of value of stakeholder engagement in terms of … working with stakeholders to create value, solve problems." (21)*

An interviewee from an international NGO who, when asked if boards are engaging with stakeholders, responded:

> *"I don't think they are! I don't think they are engaging enough, if I'm honest … it feels like there's quite a detachment from a stakeholder perspective, from a board level." (17)*

And where they are, it might be reluctantly:

> *"…they see this as a necessary evil to continue the business they have to deal with it because, you know, they rely on local workforce." (4)*

In terms of drivers for rethinking the form of stakeholder engagement, some of the expert interviewees confirmed the importance of the international rhetoric on stakeholder capitalism, particularly by the World Economic Forum:

> *"That is really influential. The World Economic Forum … measuring stakeholder capitalism document was incredibly influential amongst the large organizations, international organizations." (22)*

Other drivers include the international governance standard ISO 37000. This particular standard was mentioned by quite a few interviewees as a way to capture how stakeholder engagement should be incorporated into board-level activity.[210]

The framing of ISO 37000 includes a specific principle of stakeholder engagement (one of 11 principles) and situates stakeholders as a core part of decision-making to define organisational values and strategy; the importance of transparency with stakeholders through the use of reporting and disclosure; and the need to recognise stakeholder influence over resources, rights and expectations. The stakeholder engagement principle is that stakeholders should be "appropriately engaged and their expectations considered". The standard also refers to creating a more collaborative approach towards value generation, which indicates a much deeper engagement process than reliance on information exchange.

A stakeholder engagement consultant from Latin America said:

> *"I think that establishing a common understanding at the global level that both stakeholder engagement and social responsibility are an enabled governance principle [ISO 37000] within the system by which any organization is directed, overseen and held accountable, the standard helps recognize that society values must be taken into account and must be taken into account by the board." (1)*

Our expert interviewees also reflected on the diverse challenges and pressures that boards are facing which are driving demands for more stakeholder input. For example, pressures to deal with complex challenges at a strategic level such as the climate crisis requires:

> *"…the need to engage from having a really diverse group of individuals that are advising on your climate strategy and not … one-size-fits-all."* (15)

Another driver was considered to be materiality analysis:

> *"…you will identify the key stakeholders … you analyse what are the groups that you have to interact with, the frequency that you interact, the manner that you check for information or you track activities and so on so. It's like if you were seeing a portfolio of investments and you focus on a*

certain number of your investments, where you give more attention to this – precisely the same way. And the result of engaging with stakeholders is very rich." (5)

As a result of these different pressures, engagement can vary at the company level. For example, in the Canadian oil and gas sector, larger, multinational companies have been found to engage more deeply than smaller, more local companies, potentially due to their multi-jurisdictional pressures and prominent public presence.[211]

4.6.2.1. Refinitiv Eikon data into the extent of stakeholder engagement by companies

The figures from the Refinitiv Eikon database (Table 29) indicate that globally there has been a significant increase in the percentage of company reports that provide information on how they engage with stakeholders, how they involve stakeholders in decision-making, and what procedures are in place for stakeholder engagement. The figure rose from 36 per cent for 2017, to 54 per cent in 2021.

Table 29: Stakeholder engagement by companies

	2017	2018	2019	2020	2021	2022
% stakeholder engagement	36	39	44	48	54	(56)*

Source: Refinitiv Eikon Global Database (applicable only to large publicly listed companies); *Provisional and partial 2022 numbers

Geographically there are marked differences, with the lowest score in Northern America at 20 per cent, and the highest in the UK at 84 per cent. Looking across sectors, the highest rate is in 'Utilities' (73 per cent), possibly because they are generally regulated in the public interest; and the lowest rate, although perhaps surprising, is in 'Health care' at 20 per cent.

This data focuses on the company as a whole, and not on boards per se, reflecting the previous comments that this information could equally relate to executive activity.

4.6.3. Insights into challenges to board-level stakeholder engagement

A wide range of barriers to ensuring and enabling the right level and forms of stakeholder engagement by the board were raised in the interviews. These included: being afraid of how the market will perceive them if they engage too much; lack of willingness or understanding by the board of the need to engage; or a belief that it is time consuming and non-essential.

"I don't think a lot of businesses really understand, or directors really want to go down that path of, you know, genuinely engaging and saying: 'OK, what do you think is the best way to do this? And, you know, how can we work together to improve this?'" (21)

"From what I can observe in terms of boards, they're really struggling to make sense of these kind of new requirements in the corporate governance code and this constant push to demonstrate how they're having regard to other stakeholder groups." (21)

> *"Without the right sort of genuine intent that they do want to not only listen to stakeholders, but then actually do something with the information when it comes back, I think that's where the gap can come. You know what it's like in terms of people who are running a company, they're going to probably be strong and opinionated individuals who are looking to get a certain outcome … So, are you actually taking on board and doing something about it and reflecting it back in your strategy? I think that's where you'd have the biggest risk of a gap between intent and action." (6)*

Quite a few respondents argued that a key challenge, as already highlighted, goes back to the purpose of a business, and whether or not shareholders and profit should be prioritised.

This issue is particularly apparent in:

> *"…the advanced economies that are where shareholder primacy has been more deep rooted." (8)*

> *"I don't think there is yet a sort of settled norm and standard about what a board should be doing in relation to this, and I think that's a real gap. I think that's an area we all need to work on." (7)*

Another fundamental point raised is that there is a lack of clarity about the role of the board in relation to stakeholder engagement: what should be in the ambit of operational management; what does it mean for board oversight of appropriate stakeholder engagement processes; when and how should there be direct engagement; and when should this engagement be fully part of strategic decision-making versus more general relationship building?

One respondent had conducted an extensive global study on this topic. He said that it is important to recognise that there can be active resistance by the executive management to further involvement by the board:

> *"We heard this particularly strongly from CEOs and C suite, where they said … we don't want our boards going off and talking to stakeholders and potentially making commitments that we can't live up to." (21)*

Another motivational challenge was that appropriate stakeholder engagement is not fully incorporated into business performance incentives, as indicated by not being reflected in remuneration or compensation and with:

> *"…boards still being reluctant to set targets other than profitability targets, or financial related targets when it comes to, you know, executive compensation. So again, the … stakeholder piece is … the … weakest link in all of this." (21)*

Finally, there are also problems arising from the behaviour of some stakeholders which can act to reduce engagement or trust. For example, one interviewee noted that some major stakeholder groups, such as unions or NGOs, can have hidden agendas:

> *"We have people who don't want to negotiate. And their own stakeholders would not allow them to negotiate. That's why … with this scenario you have to cherry pick your stakeholders." (25)*

4.6.4. Emerging examples of innovation in stakeholder engagement

There are slow and emergent signs of increasing innovation in how boards engage with non-financial stakeholders. There is a limited move towards greater participation in strategic decision-making, but the general approach is through information provision and acquisition.

A challenge for organisations is determining exactly how stakeholders should be engaged; whether different mechanisms are more or less appropriate or effective for different stakeholder groups; the relative responsibilities of the board and management; and whether or not these are different for different stakeholder groups. These mechanisms are likely to differ depending on the logic adopted by the company.

The academic and interviewee data suggests that currently one-way communication, particularly via reporting and disclosure, is the predominant (and often sole) means of engaging stakeholders, suggesting a predominantly compliance approach.[212,213]

Other approaches to stakeholder engagement, most often instigated by management and not the board, were reported by the Global Reporting Initiative (GRI) to be typically in the form of: "surveys, focus groups, online forums, road shows, panels, public meetings, conferences, workshops, partnerships, one-to-one conversations, and talking to local representatives".[214]

This finding was supported by interviewees who also referred to other approaches such as community meetings with indigenous communities; employee councils; stakeholder councils; and in some cases longer-term relationships between a company and a stakeholder, for example a major environmental NGO. These mechanisms were all again mostly instigated by the management and not the board.

Our interview data included other board-specific approaches such as to:

> *"…have a temporary board member, [or] rotating board member who is representative of a particular issue or stakeholder group" (17)*

or invitations to specific stakeholders to present to the board.

Wider literature suggests that other methods are also being tried. While supervisory boards in some jurisdictions (for example Germany, or China) have a two-tier supervisory board which can include stakeholder representatives, unitary boards are also innovating. Shadow boards of younger people are being created to engage the younger workforce in strategy creation; regional or advisory boards; specific directors who are designated to understand stakeholder issues; and appointing directors who have stakeholder expertise, or are specific stakeholders (for example, Capita appointed two worker-directors to its unitary board in 2019).[215,216]

In 2019, **Interbrand**, a leading global brand consultancy, created a 'next-generation board'. This structure was not called a 'shadow board' but rather 'the Horizon Board'. It is designed to look to the future and engage 'next-gen' talent from seven cities across six continents.[217] They believe this approach is both culturally and neurodiverse, and that: "The Horizon Board is already acting as a lens through which the business looks at a number of elements in our strategy. As we live through this period of rapid transformation, the Horizon team is co-creating Interbrand's ambition and purpose. It's defining what will inspire and motivate our next generation of talent, as well as identifying the kind of talent that we want to attract in the future. It's a poignant moment for them to set our new north star."

The shareholder company model itself is also underdoing innovation to incorporate stakeholder input within a broader sustainable purpose mandate.

The British company **Riversimple**, which makes hydrogen-powered cars, embeds its purpose within a traditional company structure premised on 'shareholder primacy' but changing those shareholders to being six not-for-profit legal entities or 'custodian bodies' which are the voting equity members of Riversimple Holding Ltd. This Future Guardian Governance™ represents six stakeholder interests – the environment, customers, community, staff, investors and commercial partners. They jointly appoint the operating board, which is there to serve all stakeholders and balance their interests. To ensure stakeholder balance is maintained, there is an independent Steward's Board (effectively creating a compound board model) which is appointed by the Custodians. Its members, like non-executives, take on delegated duties, such as appointing and approving audits from the six 'benefit' streams.[218]

There is some indication that increased diversity on boards is beginning to change methods of engagement, for example, arising from women, or younger people. For example, in a virtuous cycle, women on boards are more likely to be supportive of stakeholder engagement, as well as sustainability measures.[219]

The literature search for this research found, however, that there is limited access to, or availability of, examples of how to do stakeholder engagement well, and particularly innovative methods. Additionally, any innovations that have appeared will not necessarily have been rigorously evaluated or presented with the entirety of their pros and cons, to better enable adaptation or replication by others. Ultimately the quality of stakeholder engagement can only be judged by whether it meets its intended goal.

Dual-objective (also known legally as 'dual purpose') companies, as we saw in **Phase 1: Part 2**, are other examples of bringing shareholder, stakeholder and the broader public interest value together, and, as they develop, are likely to innovate new governance arrangements.

4.7. Purpose, strategy, materiality, reporting and stakeholder engagement: concluding reflections

This section pulls together emerging themes around purpose, strategy, materiality and reporting, and reflects on their potential meaning for board practice. It also suggests implications for business sustainability using the lens of the three logics of Corporate Social Responsibility (CSR), Enlightened Shareholder Value (ESV) and Purpose driven.

4.7.1. Interim conclusions on purpose

Our evidence suggests that there is increasing discussion around purpose at board level, but that its realisation is clouded by confusion over how it is to be understood, how to forge a board–management consensus around purpose, and how to embed it within the business model. The concept of purpose as it is used in practice appears to range from literal dictionary-based definitions, to more conceptually sophisticated interpretations that link purpose to the long-term wellbeing of people and planet. Moreover, there seems overall to be a gap between thought leadership on purpose, and corporate practice.

Blending profit and purpose (in its Purpose-driven sense) potentially reframes board practice. Although we may be a long way from seeing purpose locked into the organisational DNA of all publicly listed and private companies, the discourse on purpose is clearly having some positive effects, by:

- changing the temporal outlook from short-term gains to longer-term imperatives
- expanding the scope of risk oversight
- shifting the strategic focus towards value drivers that go beyond financial return
- invigorating board-level dynamics by accommodating a broader representation of investor, workforce, societal and consumer perspectives within boardroom decision-making
- elevating board accountability standards.

Purpose has also been seen as the 'invisible leader' of business organisations, providing a unifying sense of meaning and direction.[220] Its articulation is not just found in official corporate pronouncements or glossy marketing brochures, but in the deeply rooted collective beliefs of the workforce, board and customer base of an organisation. At the moment, governing corporate conduct in a purposeful way appears to be largely aspirational. However, increased board-level engagement with the idea and implications of purpose in a growing number of companies signals an intent to reassess the alignment of corporate value delivery models with the long-term wellbeing of people and planet.

4.7.2. Purpose: implications for business sustainability

The potential of purpose to drive corporate sustainability is contingent on the interpretation of purpose, and the depth of its integration across business functions, which is differently operationalised depending on the business logic adopted:

- Business-as-usual CSR approach. These boards typically blend purpose with a trendier form of 'CSR gloss' that seeks to paint BAU practices with a more respectable veneer of ethical awareness, without fundamentally altering the underlying business model or strategic direction. While this approach can yield some short-term reputational benefits, it falls short in driving substantive change towards aligning business conduct with sustainability outcomes. This approach, if applied opportunistically, can also result in accusations of impact-washing, and over time, could undermine the goodwill of stakeholders, and increase the risk of regulatory fines and consumer backlash.
- ESV approach. Such boards can harness the synergies between corporate purpose and long-term value creation for shareholders, but this logic is ultimately contradictory. Firstly, ESV encourages a long-term view but it is, however, still rooted in the primacy of shareholder value and the corresponding commercial pressures. Every trade-off between shareholder value and purpose would ultimately be skewed in favour of the former. Secondly, ESV introduces a broader concept of corporate accountability, but this is often still tied to quantifiable metrics that have a clear link to shareholder value, rather than to societal or environmental impacts.
- Purpose-driven approach. A true commitment to purpose requires a profound reassessment of why the business exists, who it serves, and how its governance can effectively uphold its core reason for existence. A well-defined and shared business purpose can provide Purpose-driven companies with the blueprint for integrating sustainability into every facet of the organisation, aligning business success with sustainability outcomes. This is particularly true in relation to their engagement with

stakeholders. While ESV promotes a broader consideration of stakeholder interests beyond shareholders, a Purpose-driven approach goes further. It sees stakeholders not merely as groups to be heard, but as integral players in fulfilling the company's purpose. This subtle but critical difference can shift the way companies engage with their stakeholders – from a mindset of obligation, to one of collaborative (and profitable) problem-solving within system thresholds.

Purpose in these firms is not an add-on but is the fundamental reason for their existence. Purpose-driven companies put their purpose at the heart of their corporate identity, serving as the north star that shapes their vision, culture and values. The corporate purpose is tightly woven into the company's strategic framework. Business models, strategies and operational tactics are all harmonised to serve and further this purpose.

While these companies seek profitability and shareholder return, they are willing to balance these against their broader purpose. Purpose-driven companies often also embrace new ways of tracking performance that go beyond conventional financial metrics. They feed corporate sustainability data back into their strategy and operations, actively sharing data with stakeholders, aligning internal processes to learn from these feedback loops, and hold themselves accountable for their stated purpose. Finally, boards and leaders in these companies play a crucial role in safeguarding and promoting the corporate purpose. They ensure that the purpose is deeply rooted in the company's governance structure, and that decisions at all levels align with the purpose.

4.7.3. Interim conclusions on strategy

As boards become more directly involved in strategic steering, this enhanced engagement challenges the conventional boundaries of governance and management. Traditionally, boards are expected to review, approve and oversee strategies proposed by management, rather than being actively involved in shaping them. In an increasingly complex and volatile business environment, however, this hands-off approach is no longer sufficient. By being involved from the outset, boards can better understand the strategic rationale, assumptions, trade-offs and risks involved in pursuing a specific course of action. This increased involvement, however, exposes a paradox: while board-level strategic involvement can bring valuable insights, it may also encroach upon the executive management's role. Hence, there is a need to strike a delicate balance to avoid overstepping into management's territory and micro-managing. This requires clearly delineated mandates; shared agreement of strategy metrics; close bilateral dialogue; skilful directors who have operational insights about the company's business; and outstanding industry sector acumen. A delicate balance is also needed to avoid the board's strategic engagement eclipsing the board's crucial supervisory mandate. This is particularly important due to the tension that occurs when the same entity is both creating strategies and overseeing their execution.

This increased strategic engagement also requires a board with diverse skills and experience, as we have already previously discussed. Greater strategic engagement also requires significant time investment from board members, amplifying the mismatch between expanding board mandates and limited time resources. Furthermore, board members may find themselves more directly accountable for strategic failures, with all the associated commercial, reputational, or legal implications. Finally, as boards become more involved in strategic steering, this already has important implications for the frameworks which guide boards' strategic planning; what risks are considered in strategy formulation; what metrics are prioritised in evaluating success; and how this enhanced engagement intersects with the board's risk oversight and other fiduciary responsibilities.

4.7.4. Strategy: implications for business sustainability

- Business-as-usual CSR approach. Boards driven by a CSR logic will likely find it hard to engage in strategic engagement because they are resistant to bringing sustainability issues from the periphery to the core if it affects their reason for existence. Nonetheless, CSR-driven boards exhibiting more openness to strategic engagement might increasingly recognise CSR-related risks (like reputational damage or non-compliance fines) as strategic risks, which could drive more substantial efforts to mitigate them. Strategic board involvement in CSR matters, especially when mindful of broader sustainability factors, could also amplify organisational legitimacy and help build trust as a vital relational asset of the company. On the other hand, this increased involvement may also invite closer scrutiny from stakeholders, exposing the company to more criticism in case of failure to meet commitments.
- ESV approach. The boards could see merit in considering wider stakeholder interests as a means to drive long-term shareholder value. Strategic board involvement might also broaden risk perceptions to focus on new areas of non-financial risks that threaten long-term shareholder value. It could also help businesses better understand the financial risks posed by what have previously been seen as non-financial risks. This might provide better oversight of the interdependencies on which long-term enterprise survival relies. It could also call for more board attention to the symbiotic feedback loops between strategic value drivers and risk oversight. As a result, boards would be able to achieve a more nuanced equilibrium between risks and rewards, yet decisions entailing trade-offs would continue to be fundamentally driven by the quest for shareholder value, rather than sustainability outcomes.
- Purpose-driven approach. This would ensure that the company's purpose is deeply embedded in the company's strategic framework, serving as a guiding principle in evaluating strategic options and outcomes. Integrated decision-making could be used to assess strategic matters not only based on financial metrics but also on their consistency with the organisation's purpose, leading to more sustainability-aligned outcomes. Strategic engagement also empowers boards to proactively involve stakeholders in decision-making, seeking their input to inform strategic planning and ensuring that strategy execution is geared towards creating shared benefits for a wider range of stakeholders than solely the shareholders. Purpose-driven boards would also ensure transparency in the disclosure of purpose-related metrics when reporting on their progress towards fulfilling the company's strategic agenda.

4.7.5. Interim conclusions on materiality

Our evidence indicates an increase in the use of, and discussion about, materiality assessments by boards. The extent to which different understandings of materiality in a non-financial reporting context – for example, single or double materiality – are used, is harder to assess. However, a key driver of a broader scope of materiality comes partly from a backlash to poor sustainability disclosure practices, whereby important impacts were previously hidden within a plethora of minor and tokenistic positive actions.

Materiality is critical to how corporate boards conceptualise and prioritise strategic matters, which is even more salient as boards struggle to select and juggle with a proliferating range of topics that compete for board attention. Materiality assessments can provide the data necessary to unpack the strategic landscape, and be used as a decision tool, normatively informed by the business purpose. There is no convincing evidence as yet, however, which suggests that materiality assessments are actively being

leveraged as an analytic asset to inform strategy. A plausible explanation is that while in financial contexts material factors are those that are likely to alter investment decisions and affect the value of the investment, materiality criteria in sustainability reporting remain more fluid, nebulous and contested.

Quantifying non-financial factors is also intrinsically difficult. Determining which factors are material can be challenging because they might not immediately affect a company's bottom line, but can have significant impacts in the long run. Additionally, different stakeholders might prioritise different factors, making it even more challenging to define what is material. Moreover, materiality assessments should be forward-looking. Predicting future impacts, however, especially in a rapidly changing business environment, is complex and loaded with potential inaccuracies. Many materiality assessments based on stakeholder viewpoints are in fact often backward-looking since they are based on current and often narrow knowledge. Finally, if mechanically applied, materiality can sometimes lead to a 'herd mentality' whereby companies focus on a small range of issues due to industry or peer pressure, which may limit a company's ability to differentiate itself and gain materiality-informed competitive advantages.

Nonetheless, the attention to materiality assessments can have significant reverberations in board practice. Firstly, they reframe the understanding of risks away from financial risk, and help boards navigate the trade-offs between short-term gains and long-term sustainability. This careful assessment might influence capital allocation as boards may decide to mitigate slow-moving but potentially disruptive risks at the expense of short-term gains. Next, materiality assessments can catalyse the re-evaluation of what corporate success looks like, spotlighting new value drivers, and redefining the conventional metrics of corporate performance. By highlighting the most material sustainability issues, these assessments might also prompt boards to rethink the company's very business model to unlock hidden commercial opportunities arising from the sustainability transition. In addition, the slow but increasing focus on materiality also helps make visible the trade-offs involved in corporate decision-making and their distributional impacts on stakeholder groups.

4.7.6. Materiality: implications for business sustainability

- Business-as-usual CSR approach. Boards might selectively use materiality assessments to prioritise the CSR issues that can deliver the most immediate benefits to the company. Longer-term and potentially more complex or resource-intensive sustainability issues would be overlooked. CSR-driven boards may also use materiality to frame their CSR activities in a manner that highlights their contribution to sustainability, but are ultimately driven by short-term profit. For example, they may emphasise how CSR initiatives help to bolster reputation, enhance customer satisfaction, or mitigate certain immediate risks, while downplaying or ignoring the long-term strategic value of these initiatives. Boards can also distort the timeline of materiality assessments to support their short-term orientation, thereby excluding issues that might matter more in the long term. While these approaches may help boost short-term profitability, they can undermine a company's long-term sustainability, and the genuine intent of CSR.
- ESV approach. These materiality assessments will be broader in scope, focusing on a wide range of issues related to economic performance, environmental risks, social responsibility and governance standards. These assessments may provide a more comprehensive view of the company's performance and risks. Companies that are driven by ESV use materiality assessments primarily to improve financial performance, while considering the wider impacts on society and the environment. These companies acknowledge that their operations and business decisions have an impact on various

stakeholders – employees, customers, suppliers, the environment and society as a whole. Materiality assessments in this context involve identifying key risks that could materially affect the company's financial performance and shareholder value. By managing these material issues, ESV-driven companies seek to enhance their financial performance while mitigating potential side-effects that might undermine long-term value creation. An ESV approach would also be taking into account objective data on risks, and not just stakeholder views.

- Purpose-driven approach. Such boards are guided by a mission that extends beyond profit. They use materiality assessments not only to identify ESG issues that could impact financial performance, prioritising instead ESG factors based on their alignment with the company's broader purpose. Material issues for these companies are those that significantly influence their ability to make a positive impact on society or the environment. In addition to financial performance indicators, they might also focus on sustainability factors, not as a means to an end (in other words, shareholder value) but as ends in themselves.

This analysis does not mean that ESV companies ignore their broader impact, or that Purpose-driven companies ignore financial performance, but that the priority and emphasis might differ.

Moreover, Purpose-driven boards might also take a more proactive approach to materiality, seeking to shape their impact on society and the environment, while ESV-driven boards might use materiality more as a risk management tool. Although there is significant overlap between the two approaches, and many companies incorporate elements of both models into their strategy, the core motivations of ESV and Purpose-driven models differ in how they use materiality within each company. The former, ESV, seeks to align long-term shareholder value with a reduction in negative sustainability outcomes, and the more Purpose driven actively engages in addressing sustainability challenges, increasing both the stock of natural and human capital, and the wellbeing of individuals and society, in line with its unique purpose.

4.7.7. Interim conclusions on reporting and disclosure

Corporate purpose, materiality assessments and strategy execution all feed into corporate reporting and disclosure frameworks. Just like robust financial reporting builds trust among market participants, enhances market efficiency, and helps users compare financial performance to inform investment decisions, non-financial reporting provides the informational infrastructure on which the market for corporate sustainability performance relies. Our evidence shows an increasing involvement by the board in overseeing ESG and sustainability reporting and disclosure. There is also some indication that boards are slowly seeing ESG (and integrated) reporting, and the data acquisition underpinning it, as part of overall strategy development, and not just as a compliance requirement.

Exercising effective board oversight over non-financial reporting goes beyond reviewing and approving the annual sustainability report. Just like financial reporting provides the aggregate picture of all the company's activities, making accurate and meaningful non-financial disclosures that shield the board from liability involves decisions, processes and activities that cascade down most layers. Being able to report – and especially improve – on a specific sustainability metric might require a significant investment in a fixed asset, the re-engineering of a business process, the redesign of a particular job description, or the amendment of an internal document. Sustainability reporting also calls for corresponding data collection, due diligence, internal control and third-party assurance systems. Failure to do so might be interpreted as a fiduciary breach. Hence, meeting the accountability standards of this expanding area of board oversight

requires board attention and adequate resource allocation. This might also require board capacity-building and new pools of expertise, or even new board structures to oversee non-financial reporting, and the myriad bottom-up activities which are eventually reported on.

Rather than seeing non-financial reporting as an administrative burden that diverts board attention from pressing issues, the ultimate goal of reporting, in addition to providing transparency to stakeholders about performance and impact, is to serve as a decision-making tool to optimise performance on a series of metrics that are linked to the long-term survival of the enterprise and the environment in which it operates. Although greenwashing, cherry-picking, box-ticking, tokenism, complexity and diverging reporting standards continue to constrain the role of non-financial disclosures in aligning corporate success with sustainable outcomes, board leadership can make a decisive difference.

4.7.8. Reporting and disclosure: implications for business sustainability

- Business-as-usual CSR approach. Our sustainability framework suggests that the boards of companies operating under a CSR logic consider sustainability reporting and disclosure requirements as a compliance exercise and supporting their image, rather than recognising its role in informing operational and strategic change which is the impetus behind this regulation. The board might use sustainability reporting to manage regulatory risks, avoid fines, and safeguard the company's reputation from potential consumer backlash. The focus would likely be on those sustainability issues that have the potential to impact financial performance most directly and in the short term. The danger of selective disclosure and impact-washing might erode the trust of stakeholders and could expose the company to liability risks arising from misrepresentation of material information. Hence, sustainability reporting in this case would be a missed opportunity to align corporate success with sustainability outcomes.
- ESV approach. Boards operating under an ESV approach would rather embrace sustainability reporting as a strategic tool that can contribute to long-term value creation. Boards would likely use sustainability reporting to identify and manage sustainability risks, communicate with material stakeholders and build long-term relationships. They would likely be more transparent and consistent in their reporting, acknowledging not only their successes but also their challenges and failures in addressing sustainability issues. In sum, while both approaches may use sustainability reporting, the motives, depth, breadth and authenticity of the reporting can differ substantially.
- Purpose-driven approach. Sustainability reporting from a Purpose-driven board is likely to go beyond just ESG risks and opportunities to also focus on how the company's activities align with its broader purpose. In this approach, sustainability reporting is a tool to demonstrate accountability, measure progress towards fulfilling the company's existential purpose, and inspire stakeholders to support the company's mission. In this vein, Purpose-driven boards not only mitigate compliance risk but also help the executive management understand how enhanced disclosures can contribute to fostering sustainable competitive advantages. Purpose-driven boards use sustainability reporting to align their operations with sustainability outcomes, co-operate with stakeholders in solving profitable problems, and tell a compelling story of the company's impact on the world, rather than just seeking to comply with regulatory requirements and quantify ESG factors in relation to financial performance.

4.7.9. Interim conclusions on stakeholder engagement

Stakeholder engagement has traditionally been considered a managerial task, with boards taking a backseat role. However, in an era where corporate reputation is almost as scrutinised as the balance sheet, stakeholder legitimacy is key to preserving the social licence to operate. Our research suggests that there is increasing engagement by boards with the wider stakeholder ecosystem, although this trend varies by jurisdiction and there is scarce evidence of the rationales, methods, and the board versus management division of labour around stakeholder engagement.

Stakeholder engagement is a contested domain. On the one hand, denser board-level interactions with stakeholders might enhance boards' strategic oversight and risk management functions by incorporating more diverse insights and experiences. Good stakeholder relationships can also provide easier access to capital, investor goodwill and reputational gains. They can also strengthen the social licence to operate by building trust-based relational assets or social capital conducive to greater long-term corporate performance. Stakeholder engagement can also spark innovation by identifying unseen operational inefficiencies, unmet customer needs and untapped markets. In addition, stakeholders also play a crucial function in materiality assessments and sustainability reporting, both as sources of input and as monitoring agents.

On the other hand, contrarian perspectives point to how stakeholder engagement can overload board agendas, detracting directors from core governance responsibilities. Board accountability structures might also be challenged – or even diluted – as the attempt to please multiple constituencies might lead to intractable trade-offs, and stakeholders themselves may be unwilling to engage collaboratively with each other and with the board. Catering to the diverse and potentially conflicting interests of various stakeholder groups can also add another layer of complexity, costs and time pressure. Furthermore, there is a risk that boards might disproportionately focus on the loudest or most influential stakeholders, potentially overlooking the concerns of other important, but less organised and vocal stakeholders. Stakeholder engagement might lead to the politicisation of boards, as different stakeholder groups try to influence corporate decisions to favour their specific interests. This could potentially divert the company's focus away from its core business objectives.

Navigating between the advocate and contrarian perspectives on stakeholder engagement requires a delicate balance and a nuanced approach. Boards need to weigh the potential benefits against these costs in order to determine the optimal level and form of stakeholder engagement for their specific situation. Defining the engagement purpose, establishing clear governance structures, undertaking proactive outreach to less vocal stakeholders, and having a clear framework for identifying the most material stakeholders would help mitigate some of the potential challenges. Furthermore, embedding engagement in strategic review and decision-making processes rather than treating it as an additional task could prevent overloading the board's agenda, and leveraging technology might streamline engagement.

4.7.10. Stakeholder engagement: implications for business sustainability

- Business-as-usual CSR approach. Such boards might pursue selective engagement to appease the critical stakeholders who could directly threaten short-term profitability. In a business-as-usual CSR company, this engagement is also likely to only be what is demanded by powerful stakeholders, such

as shareholders. The approach taken by these boards would likely be reactive, engaging with stakeholders only when a response is necessary, such as in the wake of a crisis, during controversies, or due to pressure from activists. Publicity-driven activities with stakeholders might be another engagement strategy, as long as it allows the company to score quick wins, provide rapid response to stakeholder concerns, and enhance the external perception of the company. CSR-focused boards may also prefer ad hoc and transactional relations with key stakeholders to achieve immediate benefits or mitigate risks, although this manner of engagement might create unrealistic expectations, damage longer-term relationships, and erode relational assets. These boards may seek to shield themselves by preferring controlled stakeholder engagement channels to minimise the risk of unforeseen complications or negative publicity.

- ESV approach. These boards are likely to engage with stakeholders on an ongoing basis, not just in response to problems or pressures, to anticipate and address issues before they escalate. They may also adopt an inclusive approach to stakeholder engagement, seeking input from a broad range of stakeholders whose power, insights or relation to the company might contribute to its long-term shareholder value. ESV-driven boards might also seek to align their engagement activities with their risk oversight mandates, aiming for substantive engagement that can minimise long-term risks and secure reputational gains. These boards are also likely to engage through a variety of channels and to share information and mobilise stakeholder inputs to pre-empt value-destroying stakeholder reactions. Hence, stakeholder engagement is expected to be selectively focused on the stakeholders who can directly impact the company's long-term shareholder returns.
- Purpose-driven approach. Boards taking on this logic are likely to seek a balanced engagement with a wider range of stakeholders who have a direct interest in, or impact on, the company's purpose rather than its profitability. They would involve stakeholders in measuring the sustainability performance of the company, and the impacts related to the company's purpose, rather than financial metrics. Hence, Purpose-driven boards may engage with stakeholders in co-creating solutions and collaborative problem-solving. These boards are likely to draw on stakeholders' perspectives not only to mitigate risks and protect shareholder returns, but also to inform the strategic focus, and to understand if they are making the intended difference and how they can improve their purpose delivery rather than their balance sheet. To demonstrate their commitment to their purpose, these boards also likely to be more transparent about their activities, decisions and impacts, and establish accountability mechanisms such as stakeholder panels, ombudsmen or third-party audits to review their sustainability performance, address stakeholder grievances and improve their business practices.

5. Conclusion

The second report in this research series, *Future of Boards, Phase 1: Part 2*, explored trends in legal and regulatory frameworks for sustainability and their potential implications for board practice. It identified seven significant trends, several of which are shifting at a moderate pace, and some at a fast pace. This third report, Phase 1: Part 3, seeks to examine trends in changing board practice in response to these legal and regulatory drivers. We were particularly interested in those trends which deviate from the dominant business-as-usual (BAU) way of thinking that has been so influential in shaping business, and its associated governance practices, for the last few decades.

At this stage, the trends that have been identified are high level and largely provide an aggregate picture across the globe. However, some clear changes in board practice are apparent, especially regarding diversity in board composition; an interest in and movement towards board independence; changes in board structure, including the proliferation of sustainability-related sub-committees; and changes in which board member skills and capabilities are seen as desirable, with a growing interest in the role that group dynamics and the role of the chair play in realising the potential of these changes.

There is also evidence of increased discussion around the concept of 'purpose', but also confusion and considerable variability in how it is understood and embedded in strategy, materiality assessment and reporting. This changing landscape accompanies increasing engagement by boards with the wider stakeholder ecosystem, yet there is again a lack of clarity regarding rationales, methods and the division of labour between board and management. Nonetheless, there are discernible shifts in the scope of the board's timeframe, from a focus primarily on short-term gains to longer-term imperatives; an expanded scope of risk oversight; strategic focus towards value drivers beyond financial return; broader representation of investor, workforce, societal and consumer perspectives within boardroom decision-making; and elevated board accountability standards.

What is unclear at the moment is whether the shifts that we are currently seeing, and have identified in this research, are necessary and/or sufficient to align business success with a sustainable future. Our early analysis using the lens of the three logics of CSR/BAU, ESV and Purpose-driven offers some tentative reflections on how these trends might play out differently depending on the logic that a company and its board adopts regarding its relationship with sustainability outcomes.

Table 30: Sustainability analysis of trends/insights around 3 business logics (BAU, ESV, PDO)

Domain	Business-as-Usual CSR	ESV	Purpose driven
Board membership	Boards of BAU/CSR-driven companies would be optimised for the overriding pursuit of short-term financial returns, and board members would have been selected based on their perceived ability to achieve this. Because the characteristics associated	Boards of ESV-driven companies are likely to be motivated to alter the membership of the board as a way to better understand the broader dependencies and dynamic systems affecting the company. Such boards would likely recognise the value of multiple perspectives	As with ESV-driven companies, boards of Purpose-driven companies would be motivated to alter membership as a way to better understand the broader dependencies and dynamic systems affecting and affected by the company. Additionally, they

	with driving this type of success are more traditionally associated with a certain type of person, such boards are likely to be less diverse and the pressure to become more diverse would be harder to respond to. Diversity may not result in openly shared new insights that change board decisions.	and mindsets to devise strategy that is focused on contributing to protecting or enhancing stakeholder health and the fundamental social and environmental capital on which business activity is based.	will seek board members who have expertise and insight regarding the specific purpose that the organisation seeks to achieve.
Board structure (particularly sustainability committees)	Sustainability (or ESG) committees may be employed by BAU/CSR-driven boards as a way to contain and de-risk the growing pressure for boards to report on sustainability issues and be seen to be overseeing the issue adequately. Terms of preferential investment secured by the company may also require this level of attention. As the remit of the committee would likely be compliance or reputational based however, the committee may not penetrate the strategic decision-making of the board.	ESV boards may employ a sustainability committee as a way of ensuring adequate time, attention and expertise is focused on understanding and addressing the broader dependencies and dynamic systems impacting the company. The effectiveness of this sub-committee would depend on whether or not it is acting as a catalyst to alter board-level decisions and embed change in the business.	Purpose-driven companies would have given sustained attention to the design of both the organisation and the board that best enabled achievement of the purpose and its consequent sustainability outcomes. Where dedicated committees existed to enable focused attention (eg specific expertise and attention to the changing scientific consensus on sustainability thresholds), this would be to support every strategic consideration across all remits and functions aligning with the company's purpose and with achieving this purpose within healthy thresholds.
Board dynamics	An increased focus on board dynamics means that boards may come under increased scrutiny in future years. Any board could become victim to unhealthy group dynamics based on individual members, which is why the role of the chair is critical. However, a BAU/CSR board could have	The extent that the risks of degraded non-financial capitals, stakeholders and social and environmental systems are understood by board members may influence how far they are willing to speak freely about their views and to genuinely listen to new perspectives that fall outside of traditional	For Purpose-driven companies, as the purpose is anchored to optimising for the long-term good of people and planet, it is more likely that this 'other-serving' and urgent goal would allow individual board members to transcend individuals' fears and interests. Therefore,

	greater potential for power imbalances and groupthink, arising from the more homogenous boardroom composition that likely results from focused prioritisation of short-term financial returns. This could hinder open dialogue and constructive debate on a whole range of matters, including responding to sustainability risks and opportunities. In the wake of increased attention being paid to board dynamics and board evaluations, if such board dynamics were to be found deficient, they may attract the associated reputational risks.	board considerations. Hence, ESV-driven boards could demonstrate a move towards a more independent and inclusive dynamic, if supported well by the chair, around all decision-making including sustainability impacts and opportunities. Such a dynamic would also place a board in good stead to benefit from the increased prevalence of evaluations.	boards operating with this logic could exhibit more collaborative, inclusive and independent decision-making, if supported well by the chair. Again, such a dynamic would also place a board in good stead to benefit from evaluations, assuming those evaluations are aligned to the purpose.
Individual skills and interpersonal capabilities	BAU/CSR-driven companies would likely find the need to increase their ESG oversight and reporting skills to improve oversight of compliance duties in this area or risk increasing regulatory scrutiny. This would likely remain at the level needed to stay compliant and competent in the eyes of stakeholders however, rather than motivating upskilling in sustainability more generally, or altering interpersonal styles. This could come at the expense of attracting board members with leading-edge expertise and insight.	For ESV-driven companies, the recognition of the serious risk posed by the degraded health of the resources, systems and stakeholders the company is dependent on would likely expose gaps and deficiencies in skills and interpersonal approaches. The level and speed of effort to progress and attract suitable talent would depend on the extent to which the board understands the broad nature of the risks and opportunities faced.	Purpose-driven boards, or those committed to making the transition to being so, would be aware of the need for a level of transformational leadership skills and strengths beyond those needed for ESV, ie the skills to understand how to operate within healthy resources, stakeholders and system thresholds. This is because purpose requires leadership to actively transform (and then sustain) and align the internal and external context. They would therefore be looking to recruit and nurture the best available talent with a rich and diverse knowledge base, individual leadership capabilities and interpersonal skills, and would be best placed to

			attract those looking to deploy such talent to achieve real impact.
Purpose	If BAU/CSR-driven boards engage with purpose, it would be as a means to enhance short-term financial returns. This may include seeking reputational benefits or otherwise increasing the support of stakeholders, for example improving the productivity and retention of staff, without fundamentally altering the underlying business model or strategic direction. Implementation of the purpose would usually be centred within corporate PR, marketing or communication functions. There would be a very high risk of 'purpose-washing' for boards in this logic moving with this trend.	For ESV-driven companies, the language of purpose might be utilised but would be more about harnessing long-term financial returns creation for shareholders. Ultimately, the use of purpose would be revealed as hollow because trade-offs between shareholder value and purpose would likely be ultimately skewed in favour of the former. Therefore, there would be a high risk of 'purpose-washing' for boards operating exclusively in this logic.	For Purpose-driven boards, purpose would be used as the blueprint for integrating sustainability into every facet of the organisation. Purpose in these firms would not be an add-on, but the fundamental reason for their existence. While these companies would seek and require profitability to achieve the purpose and meet the expectations of stakeholders, they would not harness profits in a way that undermined their broader purpose, or the resources, stakeholders and systems that purpose relies on. Such companies would therefore represent the leading edge of the 'purpose' transition.
Strategy	Boards driven by a BAU/CSR logic would likely find it hard to demonstrate strategic engagement because there is no inherent rationale to bringing sustainability issues from the periphery to the core, unless this protects or enhances short-term financial returns or the precursors to this. There is the risk therefore that strategic decisions could be short-term and myopic, and ill-equipped to respond to the sustainability-related risks and opportunities with	For ESV-driven companies, strategic deliberations by the board would include contextual information about areas of non-financial (as well as financial) risks that are material to long-term financial returns. There would also be a motivation for focusing board attention on the symbiotic feedback loops between strategic decisions and risk oversight. Yet strategic decisions would be focused on optimising for financial returns, and sustainability gains that may require more creative approaches are likely to be	Purpose-driven boards would ensure that the company's purpose is deeply embedded in its strategic framework, serving as the basis of evaluating strategic options and outcomes. Integrated decision-making could be used to assess strategic matters, not only based on ensuring the health of financial stocks and flows and the health of all other capitals, stakeholders and wider systems, but also on their consistency with the organisation's purpose. This would provide a clear and

	material impact for the company in the future.	missed. Trade-offs would continue to preference financial returns over sustainability outcomes.	meaningful basis for strategic decision-making oriented to long-term value creation for both the company and wider society.
Materiality	BAU/CSR-driven companies would likely follow the trend of increasing voluntary use of materiality assessments, but the criteria used to create these assessments would likely focus on matters that are material to the firms' short-term financial return: for example the current competitive context, the material interests of powerful stakeholders, and external sustainability challenges to the extent they are judged to pose a threat to short-term financial interest. Longer-term and potentially more complex or resource-intensive sustainability issues, the non-financial material concerns of shareholders, or the concerns of less visible stakeholders would more likely be overlooked or deemed irrelevant to core strategy decisions, potentially exposing such companies to future risks and missed opportunities.	ESV-driven companies would likely see great value in increased use of materiality assessments in order to understand better the risks and opportunities for increasing the quality and resilience of stakeholders, financial and non-financial capitals, and social and environmental systems. These assessments would likely provide a more multifaceted view of the company's performance and risks that could influence long-term financial returns beyond mere ESG reporting and disclosure requirements.	Like boards of ESV-driven companies, boards of Purpose-driven firms would likely use materiality assessments to understand and manage key risks to firm-level resources (including financial), stakeholders and underlying systems. These boards, however, would likely go further in seeking to understand the impact the company has on the broader system that supports their purpose and the ultimate goal of long-term wellbeing for all (sustainability). Further, they would likely use materiality assessment to ascertain and check whether the pinnacle goal of the company (its purpose) is the optimal strategic contribution the firm can make to long-term wellbeing for all.
Reporting and disclosure	Boards operating under a BAU/CSR logic would likely take compliance with reporting and disclosure legislation seriously but would fail to appreciate the use of the information unless it was clearly related	These boards would embrace sustainability reporting as a strategic tool that can contribute to long-term financial returns. Boards would likely use sustainability reporting to identify and manage sustainability risks	As with ESV companies, boards of Purpose-driven firms would go beyond the partial range of ESG matters currently required to encompass all impacts on capitals, stakeholders and broader systems as

	to protecting or enhancing short-term financial returns. For this reason, these boards are likely to push back at trends to increase reporting and disclosure requirements, only comply to the minimum extent needed and may not proactively invest in information systems to utilise the data strategically.	and opportunities, communicate with material stakeholders and build long-term relationships to the extent these could be justified to support long-term financial returns. Because they are genuinely concerned to repair the health of their dependencies, they would push reporting and disclosure beyond the partial and mostly relative ESG requirements and seek to understand and report on the full suite of dependencies (eg all SDGs or all factors in *Doughnut Economics*). They would be motivated to lobby for further legal change to support this.	well as actively lobbying for this to be incorporated into law. Further, these boards would be using innovative reporting and disclosure systems to oversee, account for and make decisions about how the company's activities achieve the company purpose. Hence, sustainability reporting would serve as a key tool to achieve accountability, track purpose performance within healthy dependencies, establish the effective need of strategy and inspire stakeholders to rally behind it.
Stakeholder engagement	In a BAU/CSR-driven company, stakeholder engagement would likely only reflect what is demanded by powerful stakeholders. Hence, the approach taken by these boards would likely be reactive, engaging with stakeholders where a rationale to protect and enhance short-term financial returns is clear, eg in the wake of a crisis where a response is demanded. Publicity-driven activities with stakeholders (or shareholders) might be another engagement strategy. Shareholder engagement may be strong but contained to meeting their short-term financial or strategic demands. Such companies and their boards could therefore reinforce a	ESV-driven boards would likely engage with stakeholders on an ongoing basis, to anticipate and address issues before they escalate, not just in response to problems or pressures. They might also seek input from a broader range of stakeholders whose power, insights or relation to the company might contribute to the company's long-term financial returns.	Beyond the approach taken by boards of ESV-driven firms, Purpose-driven boards would likely engage with stakeholders in co-creating solutions and collaborative problem-solving to achieve the organisation's purpose within the thresholds of healthy capitals, stakeholders and social and environmental systems. Therefore, these boards would draw on stakeholders' views, not only to mitigate risks (including achieving healthy finances and expected shareholder returns), but also to understand if they are making the intended difference.

	short-term and myopic approach to strategy development.		

ss

It is also clear from this analysis that the shift towards truly Purpose-driven companies is very early and emergent, although there are signals of movement. More detailed insights into how shifts in board practice (for example, around diversity, independence, the role of the sustainability committee, strategy development, materiality analysis and reporting) are actually enabling long-term value creation for companies and wider society will help build an evidence base for action.

Further insight is also needed into the contextual elements that shape how these trends play out in different businesses. The trends in this report have largely been identified at a global aggregate level, yet early findings suggest that they vary across different geographies, sectors and jurisdictions. We are also aware that contextual factors such as sector, ownership, company size and culture are also likely to influence these trends in practice. More detailed insights into the influence of these factors will enable more tailored recommendations to companies in different situations.

Phase 2 of this research will therefore provide further insights into key selected areas of detailed board practice across a range of contexts, and provide practical recommendations for boards looking to be fit for the future.

Appendix 1

The Global Trends Survey was designed to provide an early overview of the trends facing boards around the world. It was delivered using Qualtrics software.

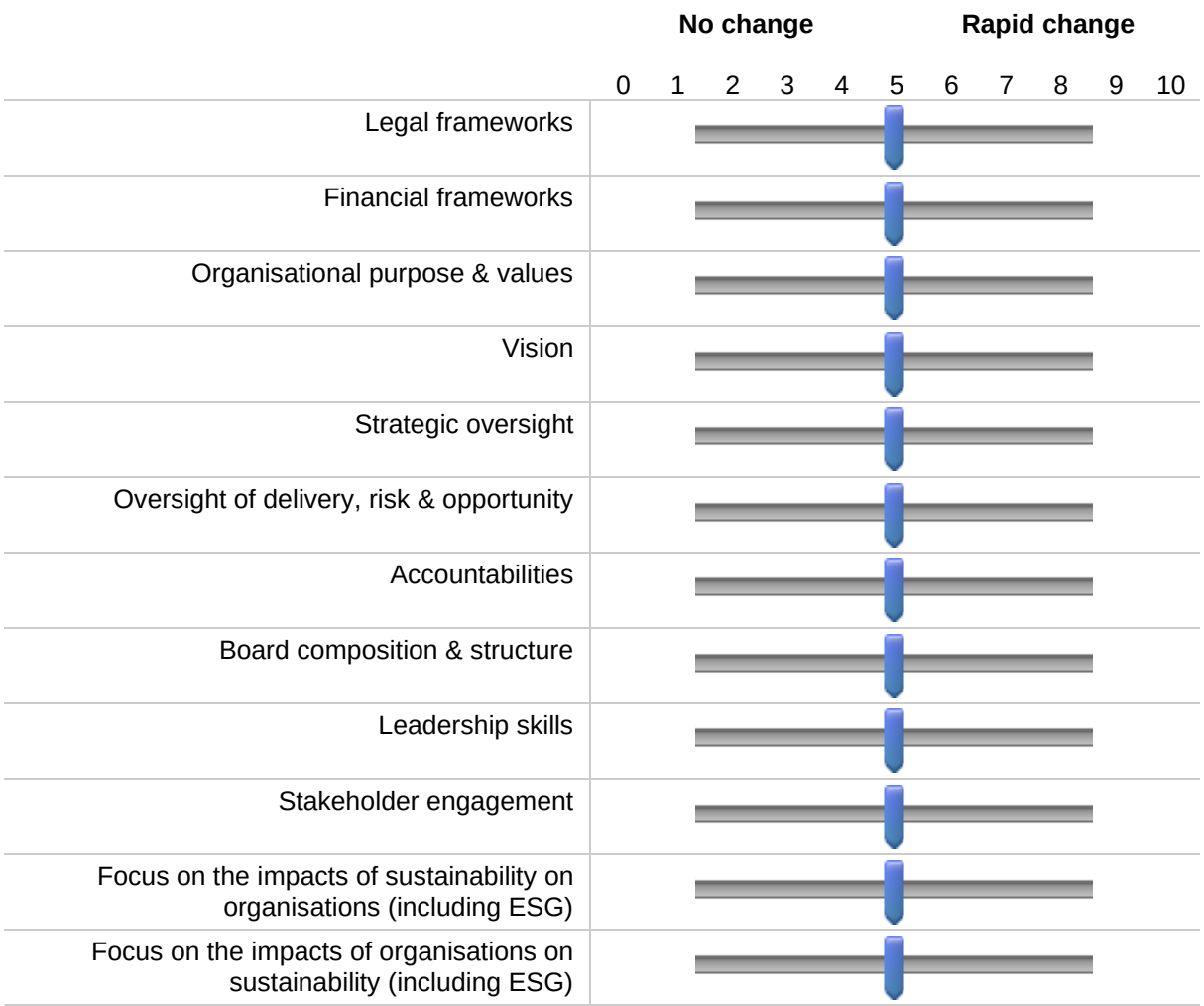
The questionnaire ran from 26 June 2022 until 30 September 2022. In total there were 433 responses, of which 102 had to be excluded from further analysis since only a few questions had been answered. The final number of valid responses was therefore 331.

Results of the Global Trends Survey

The Global Trends Survey asked respondents to identify what they thought were the strongest current trends affecting boards, as well as to comment specifically on this research's domains of interest.

The survey first asked respondents to identify the most important trends from a pre-selected list, by using a slider to indicate how fast people thought that these changes were taking place. Zero means no change, and ten means rapid change.

Figure 1: The themes used within the Global Trends Survey to enable respondents to rank their relative importance



An analysis of the replies indicated that the top three fastest moving trends, in order of the most rapid, were:

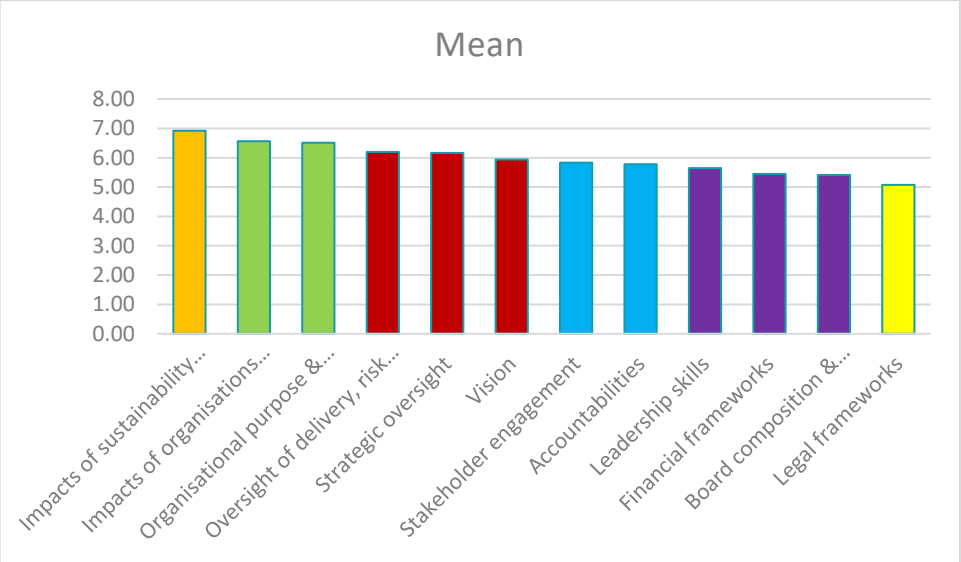
the impact of sustainability/ESG on the business (average 6.9)

the impact of the business on ESG and sustainability concerns (average 6.6)

the purpose and values of the business (average 6.5).

The responses to all the options have been grouped into coloured bands (Figure 2). These bands reflect similar mean scores, to avoid reporting an absolute ordering which is not possible since the relative importance changes slightly if the results are adjusted for the respondent's own average response tendency (in other words, the relative means of different people varied).

Figure 2: Mean scores of respondents for each trend, grouped into similar clusters



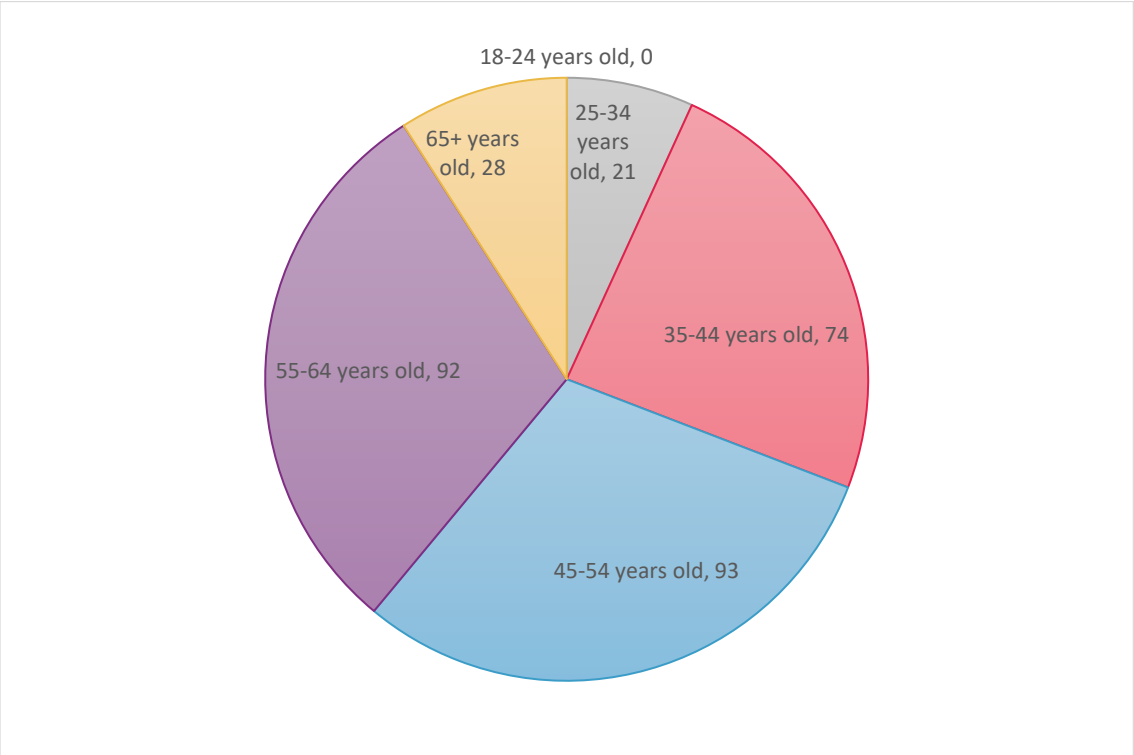
Demographics of respondents

There were about half male and half female responses (151 and 152 respectively). Five preferred not to say, out of a total answering this question of 308.

The age range of respondents was skewed more towards older working-age adults, reflecting the likely seniority of those responding (308 responded).

Age – Q20 How old are you?

N=308

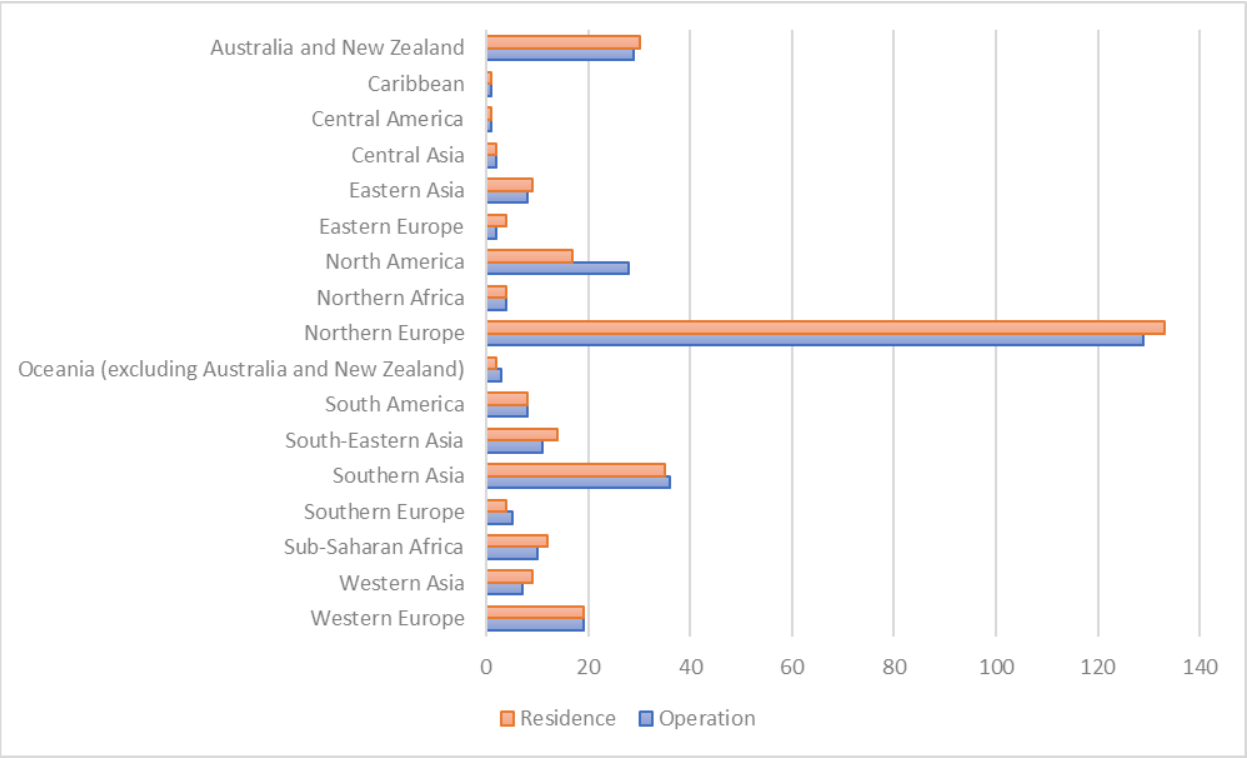


Location

The geography of the organisations they were involved with, or worked for, was spread over 57 out of 195 possible countries (29 per cent). This percentage was similar to that of the countries respondents lived in, 61/195 (31 per cent, N=303). Of the total respondents, 45, or around 15 per cent, live in a different country from their organisation (N=304).

However, looking at a more regional breakdown, there was a far higher preponderance of responses from Europe and Northern America.

N=303 (operation) / 304 (residence)



Breaking this data down further, the highest response group by far was Northern Europe, and when analysed further by country, the UK. This means that the responses from this questionnaire are not globally reflective and are therefore only indicative. They are likely to be relatively most relevant to a more Anglo-American approach to business and board behaviour, although the impact of this approach is pervasive internationally.

Job roles or positions

Looking at the different roles of respondents, half were board members, and the rest split between executive management, professional board advisors, and some shareholders, academics, board recruiters and employees.

Role – Q4 Are you: (multiple choice)

A Board member (you serve on the main governing body of your organisation, usually as a director)

An investor/shareholder

Professional Board advisor (eg a consultant, accountant or lawyer)

An academic

A recruiter for Boards

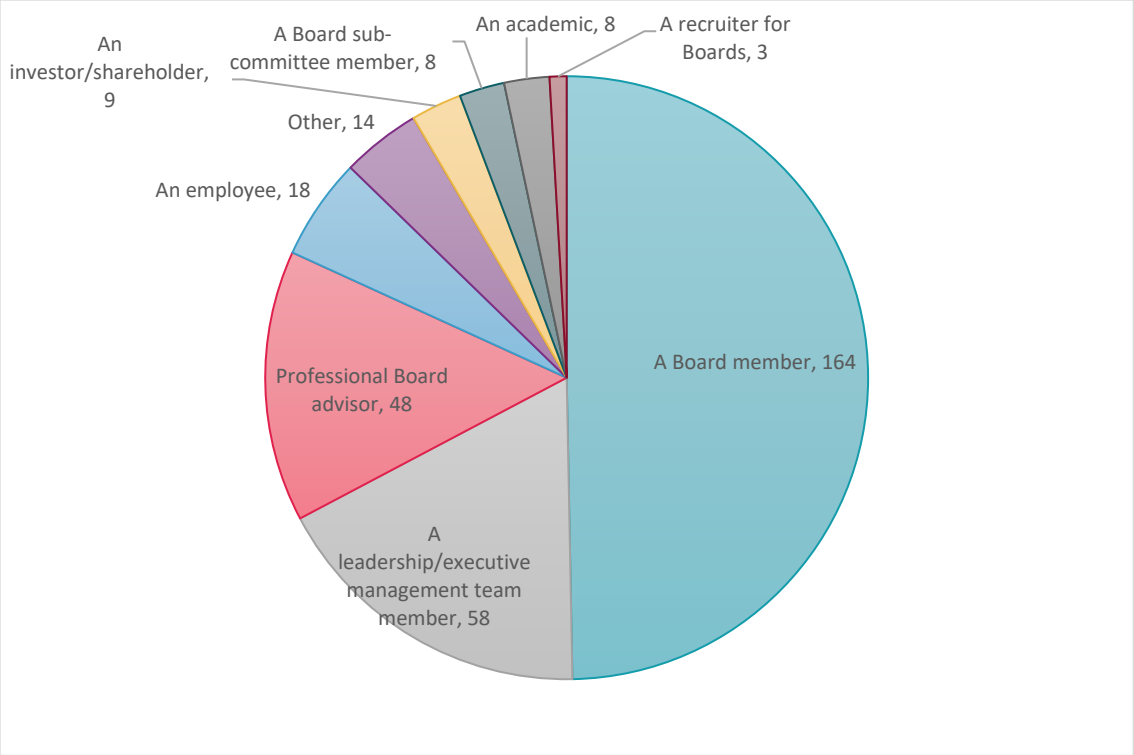
A leadership/executive management team member (and not on the main Board)

A Board sub-committee member (and not on the main Board)

An employee (and not a Board member)

Other

N=330, one respondent did not complete.



Of the board members, 62.8 per cent were non-executive and 36 per cent executive (N=330).

Of the advisors, 50 per cent were consultants, and 35 per cent lawyers (N=48).

Legal status of organisations surveyed

Most businesses were private limited companies, then public, then not for profit, and with some LLPs and a few dual-purpose companies. Others were academics, state-owned enterprises, professional bodies, or investors. It is hard to numerically quantify this answer since advisors are not part of the board, and their company structure was included in the global figures.

Industrial sectors

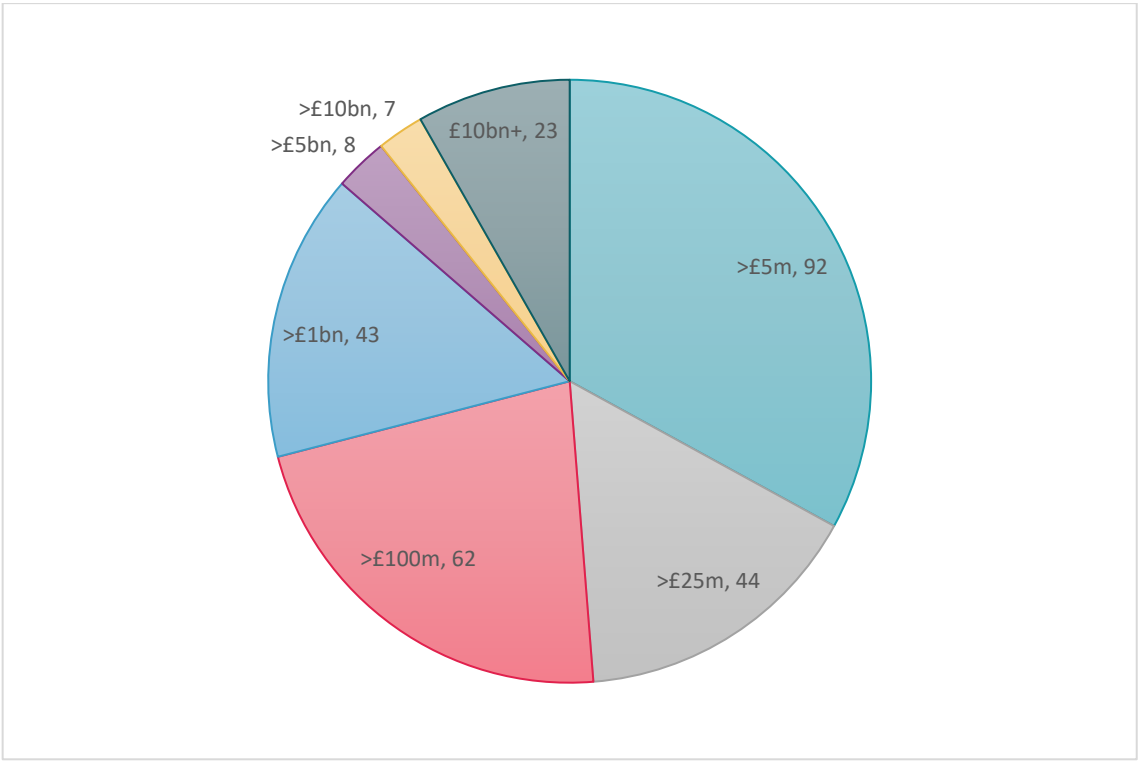
Of those respondents that answered this question (23 did not out of 308) 36 sectors were covered. Financial services were the most represented at 14.9 per cent, ICT at 8.1 per cent and education at 7.5 per cent. Again, these responses are not about the kinds of companies in which boards are found, but rather this figure is biased by the inclusion of advisory organisations.

Size of organisation

The turnover was varied, but weighted more towards larger organisations (£25 million to over £10 billion) (N=279), and with a wide range of numbers of employees (N=301).

Turnover – Q17 What is your organisation's turnover (in GBP equivalent)?

N=279, 52 no response. Non-responders potentially <£5m?


>£10bn, 7
£10bn+, 23
>£5bn, 8
>£5m, 92
>£1bn, 43
>£100m, 62
>£25m, 44

Appendix 2

The table below presents a numbered list of the interviewees with a summary of their location and/or geographical knowledge, and indicative job titles. The exact job titles are not used so that these people cannot be identified, particularly if they work for large companies and organisations. The list includes 29 individual interviewees as well as two workshops between CISL and DLA Piper which discussed emerging findings. These numbers can be used to identify the origin of the quote in the text.

Reference number	Role	Location of interviewee	Geographical knowledge
1	Governance/stakeholder engagement consultant	Argentina	Latin America
2	Reputation management consultant	UK	Global
3	Governance consultant	UK	Global
4	Board education and training provider	Singapore	South East Asia
5	Governance expert	Brazil	Latin America
6	Reputation management consultant	UK	Global
7	Governance academic	South Africa	Global
8	NED, standards, and governance expert	Switzerland	Global
9	Legal expert	UK	UK
10	Governance expert	South Africa	South Africa/Global
11	Governance/stakeholder engagement consultant	Canada	Global
12	Management consultant	UK	UK
13	Governance training provider	Trinidad	Caribbean
14	Sustainability data expert	UK	Global
15	Sustainability data expert	UK	Global
16	Sustainability data expert	UK	Global
17	Environmental NGO	UK	Global
18	Governance/stakeholder engagement consultant	Trinidad	Trinidad/Global
19	Leadership consultant and academic	US	Americas/Global

20	Sustainability consultant	Netherlands	Netherlands
21	Governance/stakeholder engagement expert	France	Global
22	Governance consultant	UK	UK/Global
23	Governance director in sustainability finance bank	US	Americas/Global
24	Governance/stakeholder engagement consultant	UK	UK/Global
25	Compliance and legal consultant	Argentina	Latin America
26	Corporate governance and strategy expert	Switzerland	Europe/Global
27	Reputation management consultant	UK	UK/Global
28	Reputation management consultant	UK	UK
29	Governance academic	UK	UK/Global
30	Governance and legal academics/legal practitioners	Group conversation – virtual	Global
31	Governance and legal academics/legal practitioners	Group conversation – virtual	Global

Appendix 3

The Refinitiv Eikon Global Companies Database data is provided as global averages as well as being broken down by broad geographical location, and by industrial sector.

Geographical location

Africa

Asia

Europe

Latin America and the Caribbean

Northern America

Oceania

UK

Industrial sector

Communication services

Consumer discretionary

Consumer staples

Energy

Financials

Health care

Industrials

Information technology

Materials

Real estate

Utilities

Endnotes

[1] International Organization for Standardization, *ISO 37000:2021 Governance of organizations – Guidance* (ISO, 2021), https://committee.iso.org/ISO_37000_Governance.
[2] Kate Raworth, *Doughnut Economics: Seven Ways to Think Like a 21st-Century Economist* (Random House Business, 2017).
[3] See for example, Florian Berg, Julian F Kölbel, and Roberto Rigobon, "Aggregate Confusion: The Divergence of ESG Ratings," *Review of Finance* 26, no. 6 (November 2022): 1315–1344, https://doi.org/10.1093/rof/rfac033; International Organization of Securities Commissions, *CR09/2021: Environmental, Social and Governance (ESG) ratings and data products providers: final report* (IOSCO, 2021), https://www.iosco.org/library/pubdocs/pdf/IOSCOPD690.pdf.
[4] European Commission (EC) and Environmental Resources Management (ERM), *Study on sustainability-related ratings, data and research* (Publications Office of the European Union, 2021), https://op.europa.eu/en/publication-detail/-/publication/d7d85036-509c-11eb-b59f-01aa75ed71a1/language-en/format-PDF/source-183474104.
[5] Victoria Hurth and Aris Vrettos, *Unleashing the Sustainable Business: How purpose transforms an organisation* (Cambridge, UK: University of Cambridge Institute for Sustainability Leadership, 2021).
[6] Friedrich A. Hayek's most influential book is *The road to serfdom*: Friedrich A. Hayek, *The road to serfdom* (Chicago, IL: University of Chicago Press, 1994).
[7] Milton Friedman, "A Friedman doctrine-- The Social Responsibility Of Business Is to Increase Its Profits," *The New York Times*, September 13, 1970, https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html.
[8] See for example, Marianna Fotaki and Ajnesh Prasad, "Questioning Neoliberal Capitalism and Economic Inequality in Business Schools," *Academy of Management Learning & Education* 14, no. 4 (2015): 556–75, http://www.jstor.org/stable/43698374, which sets out the dominant approach to business school teaching and its effect on creating global income and wealth inequality.
[9] Hurth and Vrettos, *Unleashing the Sustainable Business*.
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