Adding value

A guide for boards and HR committees in addressing human capital risks and opportunities
Table of contents

1 Human capital board oversight: evolution or revolution?
3 Key responsibilities
7 Keeping on track
13 Stepping up your game: a look at some leading practices
17 Making connections
21 Onboarding

22 Appendix 1: Sample human resource committee charter
24 Appendix 2: Human resource committee compensation approval process
25 Appendix 3: Human resource committee annual meeting planner
26 Appendix 4: Framework tool for board accountability in regard to gender diversity

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Inspired by our purpose of building a better working world, the cover art piece was created by Canadian artist Alex McLeod, working with the Contact Photography Festival.
To be truly effective, the board must address three key risks: culture, talent and strategy.
Human capital board oversight: evolution or revolution?

Boards recognize the crucial role they play in human capital matters. They learned their lesson through the major scandals of the 1990s and early 2000s and ultimately the 2008 financial crisis.

In 2011, a large-scale study was conducted into the role and effectiveness of human capital oversight among Canadian boards of directors. The vast majority indicated their boards have direct responsibility for CEO compensation, performance management and development, including succession planning. But they believed that it went further than that: boards should also monitor strategic talent management areas such as HR strategy, organizational culture, employee engagement, succession planning and development.1

Boards also acknowledge the important role talent and culture play in the company’s risk. In 2013, EY held a series of roundtable sessions with leading board members from across Canada to get their perspectives on the role boards play in overseeing risk. These discussions confirmed that a robust, systematic risk management process is a necessity, but to be truly effective, the board must address three key risks: culture, talent and strategy. It also confirmed that boards must take a broader view of risk, adopt more leading practices such as understanding and reviewing the end-to-end people strategy, monitoring its success with robust metrics and analytics and ensuring the corporate culture is a lever of corporate sustainability.

A 2014 global survey of more than 770 directors performed by McKinsey2 indicates that high-performing boards have strategy, organizational health and talent management, business risk management, core governance and compliance on their agenda.

So the question is: is this an evolution in the board’s role or is it a revolution – a dramatic and wide-reaching change?

Each organization has to define how it can best manage its human capital risks and priorities, and there is no one-size-fits-all solution. What is clear, though, is that boards are looking for ways to provide insight, oversight and foresight in matters of talent and culture. It is our belief that by developing a better understanding of their companies’ and industries’ talent capacity and issues, boards will be in a better position to support the CEO and executive team in executing their companies’ talent strategy.

“Growth is the best people strategy, but people are the only growth strategy.”

Fiona Macfarlane, Chief Inclusiveness Officer, EY

This guide is designed to assist Boards of Directors (boards) as they look to add even more value to the corporation in the area of human capital. We provide board members and human resource (HR) committees with insights to understand their evolving roles and responsibilities, as well as leading practices used by boards as they provide the value to the company in their oversight role in talent and culture.

We also offer recommendations on the relationships that are needed to expose boards to the right information and the right insights. In addition, we provide a few tools, including examples of a human resources charter, an annual meeting planner and a framework for gender diversity reporting that we hope will be helpful to boards.

Even if some of the legal requirements apply to public companies only, the leading practices set forth in this guide can be useful whether your organization is public, private or not for profit, whether it’s large or small.

1 Knightsbridge Human Capital Solutions, Clarkson Centre for Board Effectiveness and the Institute of Corporate Directors, Beyond the CEO, The role of the Board in ensuring organizations have the talent to thrive, September 2011.
Board directors have a legal duty to govern, or supervise the management of the business and affairs of a corporation. When fulfilling his or her mandate, a director must comply with the fiduciary duty and the duty of care set out in the Canada Business Corporations Act (CBCA) and equivalent provincial statutes. That is, a director must:

- Act honestly and in good faith with a view to the best interests of the corporation
- Exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances

The Supreme Court of Canada interpreted the scope of this responsibility in two judgments\(^3\) to mean that directors must act exclusively in the interests of the corporation and its stakeholders.

The Canadian Securities Administrators (CSA) have adopted corporate governance guidelines in National Policy 58-201, Corporate Governance Guidelines (NP 58-201), recommending that public company boards appoint a compensation committee made up entirely of independent directors responsible for evaluating the CEO’s performance and reviewing and approving his or her compensation, making recommendations for the compensation of other officers and directors, incentive compensation plans and equity-based plans, and reviewing executive compensation disclosure in the proxy circular.

Under National Instrument 58-101, Disclosure of Corporate Governance (NI 58-101), a public company is required in its proxy circular to either disclose that it complies with the Compensation Committee guidelines in NP 58-201 or explain why it has opted not to — the so-called “comply or explain” approach.

High-performing boards believe their responsibility is not limited to a narrow focus on CEO and senior management compensation and succession planning, but should include a robust enterprise risk management that extends to a full spectrum of human capital opportunities and risks.

The compelling business reason for this is that talent and culture are arguably the biggest drivers of innovation, growth and the ability to outperform the competition.

Talent and culture are arguably the biggest drivers of innovation, growth and the ability to outperform the competition.

The corollary to that is that human capital risks rank in a company’s top three risks.\(^4\) They exist wherever a company has employees or potential employees and wherever its people make decisions, manage, perform their job responsibilities or interact with customers.

The scope will vary from one organization to another, but they are compounded when a company undertakes business transformations such as globalization, mergers and acquisitions, outsourcing, shared service centres or restructuring. When human capital risks are managed effectively, it differentiates market leaders from average-performing companies\(^5\).

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\(^3\) Peoples Department Stores Inc. (Trustee of) v Wise (2004) and BCE Inc. v 1976 Debentureholders (2008).


Many of the potential risks identified by organizations result from either a poor alignment of the talent strategy with the business strategy (e.g., talent gaps, shortages, M&A, globalization/offshoring, use of contingent workers) or from an organizational culture that does not support desired behaviours or encourages undesirable ones (e.g., low engagement levels, ethics, excessive risk-taking, high levels of attrition).

The accompanying table ranks in order of significance a series of Human Capital risks identified by 172 global companies.

### Human capital risks ranked by significance

<table>
<thead>
<tr>
<th>Rank</th>
<th>Risk</th>
<th>% rated “very significant”</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Shortage of critical skills within the company’s workforce</td>
<td>69.9%</td>
</tr>
<tr>
<td>2</td>
<td>Compliance/regulatory issues</td>
<td>59.1%</td>
</tr>
<tr>
<td>3</td>
<td>Succession planning/leadership</td>
<td>55.8%</td>
</tr>
<tr>
<td>4</td>
<td>Pipeline</td>
<td>52.1%</td>
</tr>
<tr>
<td>5</td>
<td>Gap between talent capabilities and business goals/shortage of critical skills within the company’s workforce</td>
<td>51.3%</td>
</tr>
<tr>
<td>6</td>
<td>Employee engagement</td>
<td>49.1%</td>
</tr>
<tr>
<td>7</td>
<td>Ethics</td>
<td>43.1%</td>
</tr>
<tr>
<td>8</td>
<td>Loss of critical knowledge through attrition</td>
<td>38.7%</td>
</tr>
<tr>
<td>9</td>
<td>Labour costs</td>
<td>38.1%</td>
</tr>
<tr>
<td>10</td>
<td>Intellectual property loss or violation</td>
<td>37.7%</td>
</tr>
<tr>
<td>11</td>
<td>Managing talent through mergers and acquisitions</td>
<td>34.8%</td>
</tr>
<tr>
<td>12</td>
<td>Behaviours and practice that undermine diversity</td>
<td>32.7%</td>
</tr>
<tr>
<td>13</td>
<td>Company’s inability to compete for critical talent</td>
<td>32.3%</td>
</tr>
<tr>
<td>14</td>
<td>Excessive turnover/failure to retain critical talent</td>
<td>27.8%</td>
</tr>
<tr>
<td>15</td>
<td>Alignment of pay and performance</td>
<td>26.5%</td>
</tr>
<tr>
<td>16</td>
<td>Executive compensation</td>
<td>25.0%</td>
</tr>
<tr>
<td>17</td>
<td>Outsourcing and vendor management</td>
<td>22.3%</td>
</tr>
<tr>
<td>18</td>
<td>Globalization/offshoring</td>
<td>20.9%</td>
</tr>
<tr>
<td>19</td>
<td>Unionization/labour relations</td>
<td>16.3%</td>
</tr>
<tr>
<td>20</td>
<td>Excessive risk-taking</td>
<td>13.1%</td>
</tr>
<tr>
<td>21</td>
<td>Use of contingent workers</td>
<td>10.8%</td>
</tr>
</tbody>
</table>

The key opportunities to improve the quality of the board’s oversight over talent are:

- Assigning in-depth human capital oversight to an HR committee
- Breaking down the silos between the HR and risk and/or finance functions by developing a common language and robust analytics capabilities to give boards access to relevant information
- Giving the chief HR officer (CHRO) – the steward of human capital – more exposure to the board, to assist the board in its understanding of the human capital priorities and get a direct feel for the issues
- Adding additional human capital risks to the agenda of boards (not restricting it to executive compensation and CEO succession planning)

Human Capital matters have risen in importance to both management and boards. However, while boards recognize the importance of human capital to the business agenda, they struggle with their ability to provide insight and oversight to management. Yet other boards believe that it is the sole responsibility of the CEO and the leadership team to manage human capital.

Boards should have oversight of all business-critical risks, including human capital.

We believe boards should have oversight of all business-critical risks, including human capital. It is important to gain a deeper understanding of the talent and culture issues facing both the company and the industry for boards to be able to support the CEO and executive team in the delivery of the business strategy.

In the following pages, we look at executive compensation, succession planning and diversity and inclusion as three key responsibilities of the human resource committee and highlight some leading practices in each area. We then look into other human capital priorities that have been making the top list in the last seven years and share leading practices boards are deploying to support their organization.
Executive compensation

Most boards, even if not legislated, have an HR or compensation committee in place whose role is to set appropriate pay programs that are in the organization’s best interests and aligned with its business mission and strategy. It is leading practice for organizations to ensure that executive compensation reflects the company’s overall compensation philosophy and risk profile. The board should establish a specific set of performance objectives for the CEO annually. These should include concerns of shareholders, other investors, employees, customers and the community in which the company is located. Performance objectives should include both annual and multi-year time periods.

As a reminder, recent financial scandals have:

• Placed more scrutiny on executive compensation, thus increasing the focus on HR and compensation committees
• Prompted legislators to take a closer look at the rules surrounding executive compensation disclosure
• Reinforced the importance of risk mitigation and appropriate risk-taking consistent with the risk profile of the shareholders in compensation program design, making for sound compensation practices
• Resulted in enhanced proxy disclosure rules by the CSA and SEC
• Driven an advisory, non-binding vote by shareholders on executive compensation (Say-on-Pay) that is now a legal obligation in the US (Dodd-Frank Act of 2010) and is gaining traction in Canada

Designing a compensation plan is a mix of art and science. It needs to be tailored to the company’s particular circumstances. Both the Institute for Governance of Private and Public Organizations (IGOPP)⁶ and the Canadian Coalition for Good Governance (CCGG)⁷ have issued guidance on principles for the design and structure of executive compensation. The conclusion of the IGOPP working group on compensation is clear: it is time to redefine the composition of senior executives’ total compensation from one largely based since the 1990s on stock options. In their view, it has “wreaked havoc on many companies.”

“The best leaders challenge the status quo and seek out the visionary thinking and broad perspectives that foster opportunity and growth. We have a responsibility to tackle the complex challenges that create barriers, limit creativity and blind us to the possibilities of our talent and our organizations. There has never been a better time to drive this change; never has it been so urgently necessary.”

Gordon Nixon, Former President and Chief Executive Officer, RBC

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Many companies have been criticized for creating unsustainable income inequality between the CEO’s compensation and the average pay of their employees. Extravagant bonuses have also attracted criticism. This has negatively affected the company’s reputation and breached the trust of both their stakeholders and society at large. In many cases, CEO compensation consumes all or most of the HR committee’s agenda.

First and foremost, executive compensation needs to spur high performance and appropriate behaviour from executives. When designing executive compensation plans, boards have to balance measures of performance that take into account both quantitative and qualitative elements that may not be quantifiable but are no less critical to the company’s long-term welfare and health. An example of qualitative elements would be the key behaviours that need to be modelled to support the desired culture.

In conclusion, HR committees need to remain focused on providing thoughtful input, rigorous oversight and measured approval. Executive compensation needs to be a shared responsibility by the board overall with specific interactions with the HR, audit and risk committees.

Succession planning and leadership development

Another board responsibility that is usually assigned to the HR committee (but also sometimes to the governance and nominating committee) is succession planning for the CEO, the executive team and the board, as well as a review of the leadership pipeline.


Chartered Accountants of Canada publication, “20 Questions Directors Should Ask about the Role of the HRCC.”
In 2009, the SEC stated that succession planning is a human capital risk because of its potential high impact on business performance and continuity. Making long-term and emergency succession plans for the CEO is a fundamental board responsibility, one that should be addressed on a regular basis regardless of CEO’s health and tenure.

The reality is that few organizations have succession plans in place for the CEO and other key executives. Further, there is little monitoring of succession plans for critical positions below the CEO.\(^9\)

In fact, recent studies\(^10\) indicate that:

- Only 54% of companies reported developing a specific successor to the CEO
- 39% had no internal candidates to succeed the CEO on a permanent basis if required to do so immediately
- Companies on average spend less than two hours per year in the boardroom on succession planning-related matters
- Fewer than 60% of companies have a formal talent development plan for senior executives

A leading practice by boards is taking a strategic approach to succession planning. Ultimately, the process of succession planning helps develop talent, strengthen skills, identify gaps and reinforce strategic goals across the organization. Leading companies and their boards understand that a “talent mindset” must be part of the corporate culture for these practices to be effective.

The CCGG proposes the following best-practices for succession planning\(^11\):

- Ensure the CEO has a talent development plan in place for senior executives
- Review succession plans for the CEO and other senior executives at least annually
- Review progress against succession plans to identify talent gaps and take steps to fill those gaps through executive development or recruitment
- Ensure the board develops an independent perspective on succession and the talent pipeline
- Review with the CEO the performance of his or her direct reports
- Ensure the board has the opportunity to interact, both formally and informally, with potential senior executives

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\(^9\) Knightsbridge Human Capital Solutions, Clarkson Centre for Board Effectiveness and the Institute of Corporate Directors, Beyond the CEO, *The Role of the Board in Ensuring Organizations have the Talent to Thrive*, September 2011.


Including the CHRO in CEO and senior executive succession planning is also a notable leading practice that has developed over the last few years. The CHRO should be a key contributor in facilitating succession planning. A key success factor is to reward progress made in succession planning, including the diversity of talent available to fill key roles. The CEO needs to be held accountable by including talent development as a key performance indicator (KPI) in the executive compensation program.

**Diversity and inclusion**

Leading companies are rethinking their diversity and inclusion practices as leverage to differentiate themselves from their competitors. These companies are among the organizations that outperform competitors, with a 42% higher return on sales, a 66% higher return on invested capital\(^\text{12}\) and greater women representation on their boards and in senior leadership roles.

However, these companies are still the exception, and because of the minimal progress in the participation of women in senior roles globally, a series of international initiatives were launched to promote gender balance on company boards in developed economies by exploring the introduction of quotas, “comply or explain” regimes and other techniques to drive change.

On 15 October 2014, the Canadian Securities Administrators (CSA), announced the implementation of amendments to the existing governance disclosure rules contained in National Instrument 58-101. For financial years ending on or after 31 December 2014, non-venture issuers from seven provincial securities regulatory authorities\(^\text{13}\), as well as those in the Northwest Territories and Nunavut, will be subject to increased transparency for stakeholders and investors by providing a “comply or explain” disclosure in their proxy circulars (or in their annual information forms if no circular is sent to their security holders) regarding the representation of women on their boards and in executive officer positions.

New disclosures include:

- Director term limits and other mechanisms of renewal of the board of directors
- Policies regarding the representation of women on the board
- The board’s or nominating committee’s consideration of representation of women in the director identification and selection process

\(^{12}\) Davis report, 2011.

\(^{13}\) Saskatchewan, Manitoba, Ontario, Quebec, New Brunswick, Nova Scotia, Newfoundland and Labrador
Companies that have rethought their diversity and inclusion practices to differentiate themselves outperform competitors, with a 42% higher return on sales, a 66% higher return on invested capital and greater female representation on their boards and in senior leadership roles.

- The issuer’s consideration of the representation of women in executive officer positions when making executive officer appointments
- Targets regarding the representation of women on the board and in executive officer positions
- The number of women on the board and in executive officer positions

Fostering a higher-performing, more diverse corporate culture and mindset in Canada rather than a compliance based approach to meeting quotas will lead to more optimal outcomes. In that sense, the key success factors for this change to occur include:

- Making an authentic and visible commitment by adopting a corporate view of D&I, establishing a policy in support of D&I and disclosing the policy
- Setting the tone at the top by defining the mix of skills and diversity which the board of directors is looking to achieve in its membership, requirements for the board to establish measurable objectives for achieving diversity and for the board to assess annually both the objectives and progress in achieving them
- Setting measurable goals and indicators by linking diversity goals with business drivers and objectives to compete for talent, markets and clients
- Understanding barriers/biases and address them through an action plan
- Disclosure in each annual report the measurable objectives for achieving diversity set by the board in accordance with the balance policy and progress towards achieving them including the proportion of women employees in the whole organization, women in senior executive positions and women on the board
- Reporting on progress by the CEO and CHRO: Articulated success measures in the context of step-by-step changes and identification of how progress is tracked
- Recognizing and rewarding positive inclusive behaviours
- Embedding inclusive practices into critical business processes

Australia embarked on this journey a few years ago and achieved significant progress. Australian companies are now using a practical guide for gender balance performance and reporting.

Appendix 4 provides a framework tool for board accountability regarding gender diversity.
Talent strategy

High-impact boards invest an average of 12 hours a year on strategy, three times more than boards with moderate or low impact.14 These findings confirm the current practice that boards spend more time discussing operational details, which is a barrier for investing more of their time in high-impact talent strategy or talent-related risks.15

As global businesses become increasingly concerned about a lack of skills in key areas, treating human capital as an asset helps them to understand and plan for long-term business needs. Leading companies create an end-to-end talent strategy that links very clearly to and enables the company’s strategy. Without this, boards will find they review talent strategies piecemeal without consistent links to the business strategy.

Investing more time in talent strategy essentially means being more forward looking instead of reacting to change. Testing which talent strategy can add value allows the board to better allocate the necessary resources. It also creates a shared understanding of key potential risks.

Whether boards should have an oversight role (i.e., monitoring whether the strategic plan addresses talent-related risks and requirements) or a direct responsibility (i.e., ensuring that strategic plans address talent-related risks and requirements) is a question that is still up for debate and the answer will most likely vary based on the context of each organization. However, increasing and/or improving a board’s role in talent strategy relies on two fundamental prerequisites: the quality of the information given to the board and sufficient human capital expertise among board directors. We provide more information on this in the next section. As mentioned before, having an understanding of the organization’s long-term talent strategy is essential for high-performing governance.

As well, high-performing companies are investing in a capability called strategic workforce planning (SWP), in which the links between strategic objectives and their associated workforce implications are demonstrated. SWP is integrated with corporate strategy, business planning and financial planning: it enables HR to align human capital investments with long-term business priorities. It becomes an input to business strategy and a source of business intelligence.

Culture and organizational health

Organizations today are facing more and more demanding expectations from their own stakeholders and from the public. Companies that succeed in this environment are those that develop a clear purpose backed by a strong set of values and expected behaviours that are built into their culture — the DNA of their employees and relationships wherever they are located in the world.

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15 Knightsbridge Human Capital Solutions, Clarkson Centre for Board Effectiveness and the Institute of Corporate Directors, Beyond the CEO, The role of the Board in ensuring organizations have the talent to thrive, September 2011.
Culture is one of the most important drivers that has to be set or adjusted to push long-term, sustainable success. Culture is the environment in which your strategy and your brand thrives or dies a slow death.

Shawn Parr, Fast Company, 2012

These organizations have boards that consider culture to be a top priority and consider their role to be one of close monitoring. They have a clear understanding that their corporate culture will nurture or destroy their corporate reputation and that ethics and compliance programs are viable only if people are motivated by values and not just rules.

Successful organizations understand that their corporate culture will nurture or destroy their corporate reputation – and that ethics and compliance programs are viable only if people are motivated by values, not just rules.

Powerful metrics now exist to measure the culture and health of organizations and their impact on financial performance. Boards should expect to see the data that gives them the insight into employee engagement and culture.

Corporate culture or, simply put, “the way we do business around here,” is a key market differentiator – and a key competitive advantage.

Of the 21 human capital risks listed earlier, more than half have a direct link to corporate culture (including the risks related to ethics). These risks attest to the company’s organizational health. On the specific point of ethics, the board, as well as company leadership, is responsible for ensuring that the company it directs and governs has established the right corporate culture and that management embodies strong ethical values.

Boards are now more and more concerned with culture. Many boards are reviewing different approaches to oversee culture – either through the audit committee, ethics and compliance committee, HR committee, a specifically constituted committee or the full board.

“Great vision without great people is irrelevant.”

Jim Collins, Researcher, management guru and author of bestseller Good to Great
The CEO and CHRO should both be invited to compensation committee meetings to make sure they provide the necessary insights to the board – except for meetings that deal with the CEO’s compensation, of course.
Overseeing human capital

Whether it is an evolution or a revolution, talent and culture are now seen as key business drivers and are high on leading boards’ agendas. The overall health of the organization, its talent capacity to deliver on its business strategy and all other human capital opportunities should be integrated into the board’s agenda and adequate time should be allocated. (See Appendix 3 for an example of an annual calendar.)

The scope of human capital oversight needs to be defined for each organization based on a number of factors, such as business cycle, business strategy, nature of and appetite for risks, talent strategy and business environment.

"One of the things we often miss in succession planning is that it should be gradual and thoughtful, with lots of sharing of information and knowledge and perspective, so that it’s almost a non-event when it happens."

Anne M. Mulcahy, CEO, Xerox

Based on the company’s priorities, the board needs to develop and implement effective processes for overseeing human capital priorities, including assigning roles and responsibilities to specific committees such as the HR committee, the risk and compliance committee or a specifically constituted committee.

HR committee charter

While it is not mandatory for boards to have specific HR/compensation and succession planning committees in Canada, it is a practice that the majority of companies adopt. The HR committee charter should outline the committee’s role and duties as expected by the full board. It may also include membership selection criteria, how the chair is chosen, rotation policy and responsibilities for outside consultants. There is no one-size-fits-all for all companies and, most important, a charter should not hamper a company from delving into issues as they arise. Typically the charter includes oversight responsibility for succession planning and executive development, board and corporate diversity, benefits, HR compliance and risk management, employee engagement and non-executive compensation.

More and more, directors are looking to balance executive compensation and other matters. A leading practice is for boards to discuss executive compensation outside the November-through-February timeframe when the pressure is on. In addition they will dedicate more time for review of the key HR areas of capability building, organization climate, productivity and employee tenure.

Review of the committee charter should be done annually. Usually the charter defines a committee performance review process that allows committee members to provide feedback on the operation of the committee. It is frequent in practice to see issues and recommendations discussed completely in one meeting and decision-making and voting on a particular issue occurring at a subsequent meeting.

HR committee composition

As for any committee of the board, the HR committee’s chair and composition are both important parts of its effectiveness. The CSA recommends that all members of the compensation committee should be fully independent for public companies, even though in practice HR committee assignments are still largely influenced by the chair or CEO. Consider selection of compensation committee members through the nominating committee, corporate governance committee or some full board process to reinforce the independence of HR committee chair and members.
Progressive boards rotate committee members every three to five years. Committee chairs may stay on for one year to provide continuity. Companies should improve new member orientation, especially if members are rotated. (For examples of information and data for a new HR committee member, refer to the Onboarding section on page 21.)

**Human resource expertise**

The lack of skill and expertise in HR matters continues to be identified as a barrier to board effectiveness in human capital matters. The HR committee chair, in particular, needs to have strategic human resources experience and expertise as well as fundamental compensation experience since he/she sets the committee agenda. It is estimated that fewer than 20% of boards have a director with human capital expertise. To acquire the necessary HR insights, boards have to rely on non-board members invited to the meetings. Going forward, this should be addressed.

A compelling case can be made that CHROs should attend most, if not all, board meetings. Just like CFOs, the CHRO is responsible for one of the most important corporate assets. In addition to having the CHRO present at board meetings, organizations should have an independent board member who is proficient in HR matters. The combination of these two elements will make for a more effective board as there will be a strategic look at human resource priorities.

An independent member needs to have strategic HR experience as well as fundamental compensation experience. A board member with experience in talent matters who can engage in a dialogue with the CHRO and has the ability to ask the right questions of the right people is critical to a high-performing HR committee. As well, since ethics and values are at the forefront of most companies, the board’s culture is also an important element in having the company’s values visible and embedded. The board chair sets the tone for the board culture and ensures it aligns with the organization’s values.

**MAKING CONNECTIONS**

CHROs have spent at least 30% more time with the board of directors since the financial crisis, playing an important advisory role in executive pay, succession planning and risk management.

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16 _The Compensation Committee Of The Board: Best Practices For Establishing Executive Compensation_, Conference Board, 2001, and _Beyond the CEO, The Role of the Board in Ensuring Organizations Have the Talent to Thrive_, Knightsbridge Human Capital Solutions, Clarkson Centre for Board Effectiveness and the Institute of Corporate Directors, September 2011.

Greater involvement from the CHRO

The financial crisis and significant CEO turnover have propelled executive pay, succession planning, governance and risk management to the forefront of the board’s agenda. This has put pressure on the CEO and the CHRO. In fact, CHROs have reported spending at least 30% more time with the board of directors than in the past,18 playing an important advisory role in these matters. In order to be efficient in his or her advisory role, the CHRO needs to come to board meetings with human capital metrics and analytics that guide business decisions based on data that articulate the organization’s capabilities and capacity.

The HR committee needs to be comfortable that the CHRO has the skills necessary to manage the company’s talent and culture issues.

HR leaders are also responsible for instilling, protecting and enforcing the organization’s ethics and corporate values. However, the entire organization looks to the CEO for the tone from the top. The CHRO is an important facilitator and counsel in this matter and needs to work closely with the HR committee chair to make sure the corporate values are modelled by the board members as owners of corporate reputation. The CHRO’s ability to solve the people issues helps the company become more successful, and that of course is critical to the board.

Working with outside consultants

Just as the external and internal auditors provide insight and advice to the audit committee, leading HR committees have an external advisor who understands the business strategy, can help provide insights into leading practices and be a sounding board for the HR committee.

It’s important to develop open communication with the HR consultant and the CHRO. While the HR advisor works for the HR committee, they need to work with the CHRO. There can’t be any surprises on either side. The committee should judge when and what type of outside advisor it needs to fulfil its responsibilities. The outside consultant should report to the committee, although they may be hired to provide consulting services to management as well.

It is also considered a leading practice to have a periodic audit or peer review of the company’s compensation plans by another outside firm.

While the entire organization looks to the CEO for the tone from the top, HR leaders are also responsible for instilling, protecting and enforcing the organization’s ethics and corporate values.
Adding value: a guide for boards and HR committees in addressing human capital risks and opportunities
The HR committee chair is responsible for providing orientation to new committee members with respect to their duties. Each member will have, or will acquire within a reasonable period of time following their appointment, a thorough understanding of issues related to human resource and executive compensation.

Here is a non-exhaustive list of issues that can be of importance to the HR committee:

**Functioning of the HR committee**
- The human resource committee’s requirements and objectives and the timing of reporting requirements (refer to Appendix 3)
- HR charter and recent HR committee meeting minutes

**Understanding the business context**
- Corporate mission or purpose
- Company’s business and its industry
- Company’s products and services
- Business strategy and annual business plan and financial objectives
- Management philosophy, culture, values and expected behaviours and code of conduct
- Organizational structure

**Understanding the human resources context**
- Talent demographics and geographies
- Long-term talent strategy and end-to-end annual talent plan, including objectives and metrics
- Compensation philosophy, total rewards strategy including reference markets and benchmarking methodology, compensation structure including short-term and long-term incentive plans, benefits and retirement plans
- Employer brand and employee value proposition
- HR corporate dashboard
- The labour environment, union contracts, outsourcing facilities
- Health and safety strategy and compliance
- Operational HR risks
- Key HR policies and any principles and practices unique to the company’s industry, including succession plan and pipeline, diversity, talent development
- Pending HR litigation or contingencies or labour conflicts
Appendix 1: Sample human resource committee charter

1. Definitions
In this document:
1.1 “Board” means the Board of Directors of the Corporation;
1.2 “Corporation” means Company ABC;
1.3 “HR Committee” refers to the Human Resource Committee.

2. Role of Committee Chair
a. The Board appoints the Chair of the HR Committee from among the directors of the Board;
b. The role of the HR Committee Chair is to oversee the effective functioning of the committee and to demonstrate leadership and awareness in ensuring the committee's work is a representation of best Human Resource practices.
c. The Chair ensures that each member of the committee has the necessary mix of skills and experiences to exercise his/her role and has received the necessary onboarding training.
d. The Chair ensures effective and transparent communications between the committee and the CEO and plays an active role in setting the tone at the top in terms of ethics, transparency and aligning board directors' behaviours to the corporate values.

3. Mandate
Subject to the powers and duties of the Board, the mandate of the HR Committee is to review, report on and, if required, make recommendations to the Board or management on matters relating to human resource, corporate diversity as well as the representation of women on the board, compensation policy and to establish a plan of continuity and development of senior management for the Corporation.

4. Membership
4.1 The HR Committee may, from time to time, appoint advisors to the HR Committee who are not directors of the Board, but who possess skills or experience that would be of ongoing benefit to the HR Committee in carrying out its mandate.
4.2 The Chief Human Resources Officer of Company ABC or a person responsible for substantially like matters of Company ABC shall be entitled to attend, discuss and receive all materials for meetings of the HR Committee, as an observer only, without any vote on matters before the Committee.
4.3 The Chair of the Audit/Risk Committee shall be a member of the HR Committee.
4.4 The Committee shall be composed of not fewer than three independent directors and not more than four. The President and CEO shall be excluded from the member selection process.

5. Meeting Procedures
5.1 The quorum for meetings of the HR Committee is a majority of the members.
5.2 Meetings of the HR Committee may take place by telephone.
5.3 In the absence of the Chair from any meeting of the HR Committee the remaining members may choose a Chair from among them and proceed with the meeting, provided that the quorum is met.
5.4 Favour reaching a consensus by having open and complete discussions.
5.5 Each member of the HR Committee shall have one vote on each matter to be decided.
5.6 All decisions of the HR Committee shall be decided by a majority vote.

5.7 The Chair of the HR Committee shall have a second or casting vote.

5.8 The HR Committee shall keep minutes of its meetings that record all actions and decisions taken by the HR Committee and these minutes shall be submitted to the Board as soon as is reasonably possible thereafter.

5.9 The HR Committee may appoint one of its members, the Corporation’s Corporate Secretary or Assistant Corporate Secretary, or any other person to take the minutes of its meetings.

5.10 The Corporation will provide support services required by the HR Committee.

5.11 The HR Committee shall meet as frequently as it determines necessary provided it meets at least four times per year.

5.12 An annual calendar of the meetings shall be established at the beginning of each year in collaboration with the CEO and CHRO; the compensation approval process and the HR Committee planner shall also be established (see Appendices 2 and 3).

5.13 The time and place where the meetings of the HR Committee are to be held and the procedure at such meetings shall be determined solely by the HR Committee, except as otherwise established herein.

6. Duties and Responsibilities

Oversight of executive management compensation, performance assessment and succession planning

The duties and responsibilities of the HR Committee include the following:

6.1 Monitoring executive management’s performance assessment, succession planning and compensation;

6.2 Ensuring that appropriate mechanisms are in place regarding succession planning for the position of the CEO;

6.3 Ensuring that the CEO has put into place and monitoring, succession planning systems and policies for management, including processes to identify, develop and retain the talent of key contributors;

6.4 Recommending appointment of executive management and approving the terms and conditions of their appointment and termination or retirement;

6.5 Reviewing corporate goals and objectives relevant to the President and CEO, evaluating the CEO’s performance based on those goals and objectives and such other factors as the Corporation and HR Committee deem appropriate and in the best interest of the Corporation and its stakeholders, and recommending the CEO’s compensation based on this evaluation, for approval by Independent Board members;

6.6 Reviewing the evaluation of executive management’s performance and recommending to the Board executive management’s compensation;

6.7 Overseeing the selection of any benchmark group used in determining compensation or any element of compensation and reviewing disclosure on such group.

6.8 Overseeing the identification and management of risks associated with the Corporation’s compensation policies and practices and reviewing disclosure on the role of the HR Committee in that respect; the identification of the risks and the mitigating practices;

6.9 Reviewing and making recommendations to the Board for approval, the development of new or revised salary structures and incentive plans;

6.10 Recommending pension plan design to the Board;

6.11 Selecting independent compensation consultants to advise the committee, when appropriate, on issues such as selecting an appropriate peer group, plan design, satisfying the regulations regarding compensation disclosure and setting performance measures.

Oversight of Human Resource practices

6.12 Review the end-to-end annual talent strategy and plan, workforce plan, goals and objectives, and progress report indicators and report to the Board on potential risks or gaps in resources.

6.13 Annually review the employee engagement evaluation.

6.14 Annually review the Organizational Structure and the management Succession Plan.

6.15 Review the Labour Relations Strategy and provide recommendations to the Board for approval of collective bargaining mandates.
6.16 Review the Health and Safety Strategy and compliance. Provide recommendations to the Board for approval with respect to changes in and appropriateness of policies in place to administer health and safety programs, standards and accountabilities.

6.17 Review the diversity and inclusion plan and goals of the organization.

6.18 Annually review and recommend changes to the Committee’s mandate.

6.19 Review as required any notifications sent to the Code of Ethics Hotline and follow up on their resolution.

6.20 Any other matters which come before the HR Committee in the course of carrying out its mandate.

6.21 Overseeing that the processes are in place to evaluate the performance of the HR Committee and the overall Board effectiveness (in the absence of a Board Corporate Governance and Nominations Committee).

6.22 In reviewing annual Board performance and effectiveness, the HR Committee will consider the balance of skills, experience, independence and knowledge on the Board and the diversity representation on the Board, including gender, how the Board works together as a unit, and other factors relevant to its effectiveness.

Appendix 2: Human resource committee compensation approval process

<table>
<thead>
<tr>
<th></th>
<th>Recommend</th>
<th>Review</th>
<th>Approve</th>
</tr>
</thead>
<tbody>
<tr>
<td>President and CEO</td>
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<tr>
<td>All compensation</td>
<td></td>
<td>Chair and/or HR Chair</td>
<td>HR Committee</td>
</tr>
<tr>
<td><strong>Executive (other than CEO)</strong></td>
<td></td>
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</tr>
<tr>
<td>Salary ranges</td>
<td>President and CEO</td>
<td>HR Committee</td>
<td>Board</td>
</tr>
<tr>
<td>Salaries</td>
<td>President and CEO</td>
<td>HR Committee</td>
<td>Board</td>
</tr>
<tr>
<td>Incentive/bonus plans</td>
<td>President and CEO</td>
<td>HR Committee</td>
<td>Board</td>
</tr>
<tr>
<td>Incentive/bonus payments</td>
<td>President and CEO</td>
<td>HR Committee</td>
<td>Board</td>
</tr>
<tr>
<td>Benefits/perquisites</td>
<td>President and CEO</td>
<td>HR Committee</td>
<td>Board</td>
</tr>
<tr>
<td><strong>All other management staff</strong></td>
<td></td>
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</tr>
<tr>
<td>Salary ranges</td>
<td>President and CEO</td>
<td>HR Committee</td>
<td>HR Committee</td>
</tr>
<tr>
<td>Salaries</td>
<td>Vice President</td>
<td>President and CEO</td>
<td>President and CEO</td>
</tr>
<tr>
<td>Incentive/bonus plans</td>
<td>President and CEO</td>
<td>HR Committee</td>
<td>Board</td>
</tr>
<tr>
<td>Incentive/bonus payments</td>
<td>Vice President</td>
<td>President and CEO</td>
<td>President and CEO</td>
</tr>
<tr>
<td>Benefits/perquisites</td>
<td>President and CEO</td>
<td>HR Committee</td>
<td>Board</td>
</tr>
</tbody>
</table>
### Appendix 3: Human resource committee annual meeting planner

<table>
<thead>
<tr>
<th>Item</th>
<th>March</th>
<th>May</th>
<th>August</th>
<th>November</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Total rewards strategic review (includes philosophy, guidelines, competitive status)</td>
<td>✔</td>
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<tr>
<td>2. Short-term and long-term incentive plans (STIP/LTIP) policy review</td>
<td>✔</td>
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<tr>
<td>3. Executive prior-year performance evaluation and incentive payments approval</td>
<td>✔</td>
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<tr>
<td>4. Establish current-year targets for STIP/LTIP</td>
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<tr>
<td>5. Review CEO performance criteria and protocol</td>
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<tr>
<td>6. Review the HR Committee terms of reference and rolling agenda</td>
<td>✔</td>
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<tr>
<td>7. Employee engagement survey report</td>
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<tr>
<td>8. Review pensions status and governance</td>
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<td>✔</td>
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<tr>
<td>9. Review the annual talent strategy</td>
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</tr>
<tr>
<td>10. Review the strategic workforce plan</td>
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<td>✔</td>
<td></td>
</tr>
<tr>
<td>11. Review and monitor HR dashboard</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
</tr>
<tr>
<td>12. Review the management and CEO succession plan</td>
<td>✔</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>13. Conduct CEO performance review</td>
<td>✔</td>
<td></td>
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<tr>
<td>14. Benefits review</td>
<td></td>
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<td>✔</td>
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<tr>
<td>15. Review the corporation’s safety and health strategy</td>
<td>✔</td>
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<tr>
<td>16. HR corporate risks</td>
<td>✔</td>
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</tr>
<tr>
<td>17. Review the labour relations strategy</td>
<td>✔</td>
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</tr>
<tr>
<td>18. Review the diversity and inclusion agenda and status</td>
<td>✔</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>19. Integrity line reporting</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
</tr>
<tr>
<td>20. Labour relations update</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
</tr>
</tbody>
</table>
## Appendix 4: Framework tool for board accountability in regard to gender diversity

Source: 2013 Guidelines for Gender Balance Performance and Reporting Australia\(^\text{19}\)

<table>
<thead>
<tr>
<th>Level 1</th>
<th>Getting started</th>
</tr>
</thead>
<tbody>
<tr>
<td>Develop and disclose a diversity policy and action plan</td>
<td>Annual report and/or website to include a summary of policy and annual assessment</td>
</tr>
<tr>
<td>Annual reporting of the proportion of women employees in the whole organization, women in senior executive positions and women on the board</td>
<td>Annual report and/or website to include metrics as indicated below or applicable percentages</td>
</tr>
<tr>
<td>Disclosure of board selection process – a statement as to the mix of skills and diversity for which the board is looking to achieve membership of the board</td>
<td>Annual report and/or website to include a summary of process</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Level 2</th>
<th>Getting there</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual reporting of measurable objectives as set out in the policy for achieving gender diversity</td>
<td>Annual report and/or website to include objectives</td>
</tr>
<tr>
<td>Annual reporting of performance against measurable objectives</td>
<td>Annual report and/or website to include performance against objectives</td>
</tr>
<tr>
<td>Publicly stated gender targets for women in management and senior executive positions</td>
<td>Annual report and/or website to include targets</td>
</tr>
<tr>
<td>Internal procedures to review effectiveness of diversity policy</td>
<td>Gender balance dashboard/scorecard</td>
</tr>
<tr>
<td>Procurement policy includes guidelines for supplier and outside providers reporting on workforce gender composition as a minimum threshold for doing business</td>
<td>Gender balance dashboard/scorecard</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Level 3</th>
<th>Getting serious</th>
</tr>
</thead>
<tbody>
<tr>
<td>Key performance indicators (KPIs) on gender balance targets included in annual performance scorecards for CEO</td>
<td>Gender balance dashboard/scorecard</td>
</tr>
<tr>
<td>KPIs on gender balance targets included in annual performance scorecards for all managers</td>
<td>Gender balance dashboard/scorecard</td>
</tr>
</tbody>
</table>

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