A CORPORATE BOARD MEMBER/EY RESEARCH REPORT

HOW TODAY'S BOARDS ARE TRANSFORMING FOR TOMORROW

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Boards find themselves operating in an era of near-perpetual volatility and uncertainty coming off the COVID-19 pandemic and amid geopolitical upheaval and quickly developing emerging technologies, all of which have led directors to interact with each other and execute their oversight in new ways. Waves of change have swept boardrooms in the past, but usually in the aftermath of major corporate crises and new regulatory requirements. This time, however, is different. As boards face new pressures and new tasks, many are taking a more proactive approach to change the way they get work done.

Of course, this is just the beginning—generative artificial intelligence (AI), new virtual meeting technologies and more innovations are already at work in some boardrooms or seem to be just around the corner. To better understand the shifts directors and their boards have already taken in the early 2020s, and how they will impact the boardroom of tomorrow, Ernst & Young LLP (EY) and *Corporate Board Member* worked together to survey more than 250 US corporate directors representing a wide range of companies across industries. Below we review the results of this survey and then identify how directors may think about making the trade-offs necessary for successfully implementing many of these changes.

IN BRIEF

Corporate boards have undergone a significant restructuring of how they work in the face of successive waves of disruptive changes.

Directors seek more discussion time on strategic matters and less time on routine matters.

Boards are exploring trade-offs to alter their agendas and how they get work done.

Boards are proactively adapting to the business environment of the 2020s and beyond

In the recent past, boardroom changes were often driven primarily by legislative and regulatory requirements.

In 2002, the Sarbanes-Oxley Act elevated the importance of the public company audit committee, requiring it to include independent members and financial experts and to exercise greater oversight of the firm's financial controls. Less than a decade later, the Dodd-Frank Wall Street Reform and Consumer Protection Act placed a larger focus on board oversight of risk and on changes to disclosure of executive compensation, which in turn spurred an increase in overall transparency in proxy communications. Recent Delaware court decisions, such as *Marchand* and *Boeing*, have aimed to hold directors responsible for more direct oversight of a company's critical risks.

Many boards are now making proactive changes in response to stakeholder expectations and taking advantage of new technologies.

Boards now face a critical inflection point. The regulatory environment in the US and globally continues to evolve, and companies are keeping pace. In addition to expected new regulation, an increased emphasis on materially important social issues and environmental concerns, rapidly developing AI technologies, and the use of virtual meetings are changing the look and feel of the corporate boardroom. Many boardroom changes in the last few years have been a result of director attention to investor expectations, as well as boards' desire for continuous improvement. Boards are now using virtual meetings and meeting more often to address a broader set of topics. They are also changing how they engage with management, stakeholders and each other. The exact nature of these changes is unique to the circumstances and needs of each board. For many boards, these changes have significantly changed how work gets done. As a result, their agendas are different, their members have different skills, they hold different relationships to the business, and they ask different questions of management.

Key points in the evolution of the boardroom in the last 100 years

1934
Following the Great Depression, the Securities and Exchange Act of 1934 creates the SEC to protect investors by requiring consistent and comparable disclosures, among other things, to enable investors to make wise choices.

1970
The Penn Central bankruptcy surprises its board of directors, kicking off the movement to create more independent directors.

1992
Portable Document Format (PDF) enables the digital board book.

InSoft's Unix-based videoconferencing software, Communique, enables virtual board meetings.

2002
Sarbanes-Oxley improves board oversight of financial statements by requiring audit committees to approve a wide variety of audit and non-audit services as well as the selection and oversight of the firm's external auditor.

2010
Dodd-Frank improves board oversight of risk and transparency in executive compensation following the Great Recession by giving shareholders greater access to proxy materials to nominate directors, a vote on executive compensation and new independence requirements for compensation committees.

2020 to present
Boards are adapting to continued increases in investor and other stakeholder expectations of directors, as well as the aftermath of the global pandemic, recession, and geopolitical events; regulatory initiatives in cyber and environmental, social and governance (ESG); and titanic shifts driven by unprecedented emerging technologies. Many of these boardroom changes are being made absent a specific regulatory requirement.

Source: EY Center for Board Matters research

BOARD ADAPTATIONS IN AN ERA OF PERPETUAL DISRUPTION

Key board takeaways

• According to our research, in the last several years, three in four boards initiated at least three substantial and permanent changes to the way they operate. COVID-19 drove many of these changes, and most are here to stay.

• Despite strong agreement on what the key risks are, directors report misalignment with management on short- and long-term risk appetite and suggest this is an area where they need improvement.

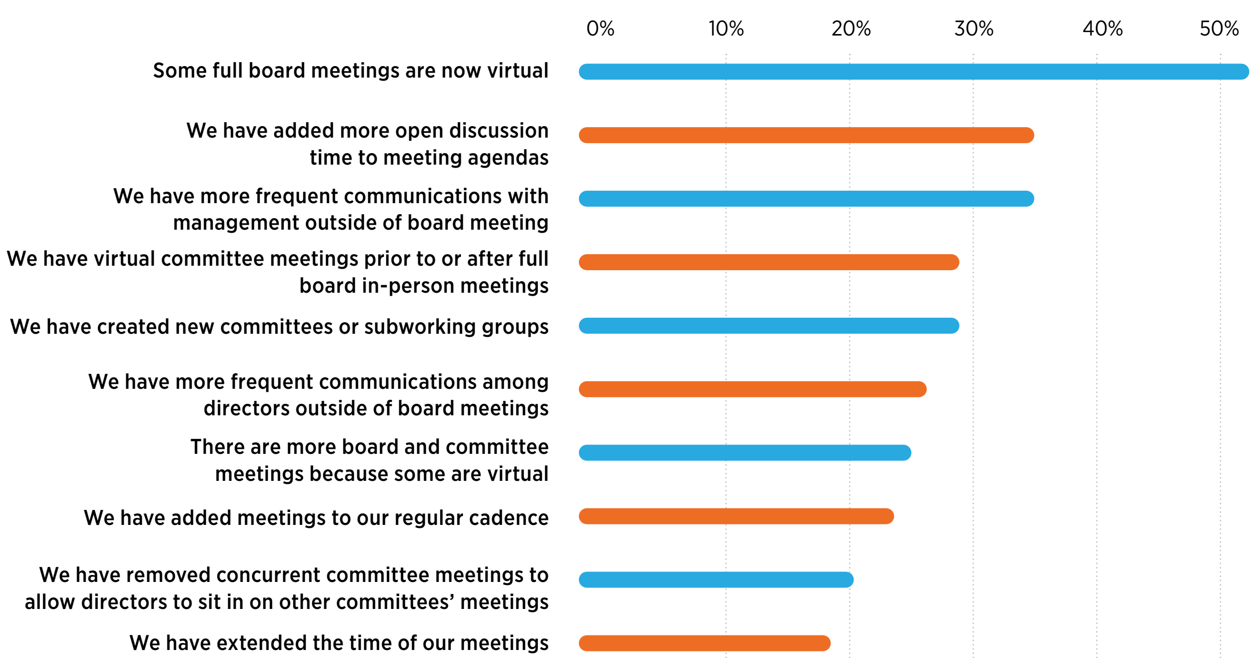
• Many boards are seeking ways to create more time for discussions and reduce the time for routine and backward-looking information reported by management.

The role of the board continues to be challenging with both evergreen and new topics continuing to come onto the board's plate. Recently, these topics included ESG matters; diversity, equity and inclusion; the talent agenda; and evolving regulatory requirements. Other topics such as cybersecurity and disruptive technology are not new, but they require constant diligence to keep up with. At the same time, expectations from all stakeholders seem to be growing. Directors are cognizant of the impact on the board—as well as on management—of further expanding the board's time commitment to address these topics, and yet nothing seems to ever come off the board agenda.

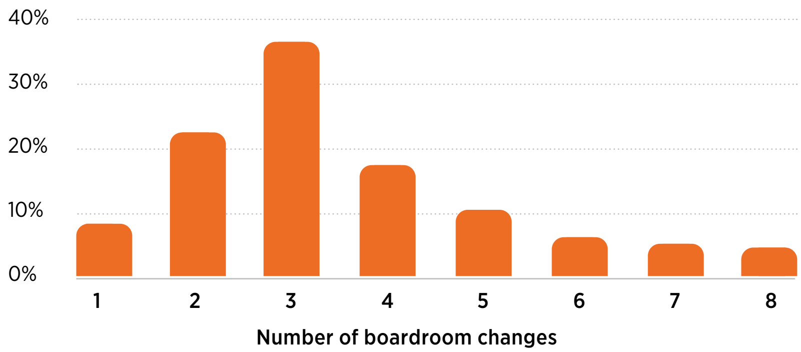
Boards are changing how they meet and how that meeting time is spent, and engaging more outside the meeting structure.

In our survey, we asked directors to identify which of 10 changes they have made to their board meetings in the last three years. Seventy-one percent of directors report they made at least three changes. When we asked directly if their boards are actively working to transform the structure of the board agenda (e.g., adding more time for open discussions, or more time for sessions with only independent directors), more than half (54%) said that they are.

Percentage of directors reporting selected board meeting changes in the last three years



Percentage of organizations making a specified number of boardroom changes



Directors seek more time to engage with management—and each other.

To help identify how directors would prioritize further changes, we asked them to consider what they would add if they had two additional hours at a board meeting. Survey responses indicated that board members are seeking ways to adapt the work of the board in response to a complex, uncertain business environment. Directors reported that if they had more time they would add more discussion (60%), more time for directors to engage with management and employees (46%), and more time to discuss new and emerging issues (35%).

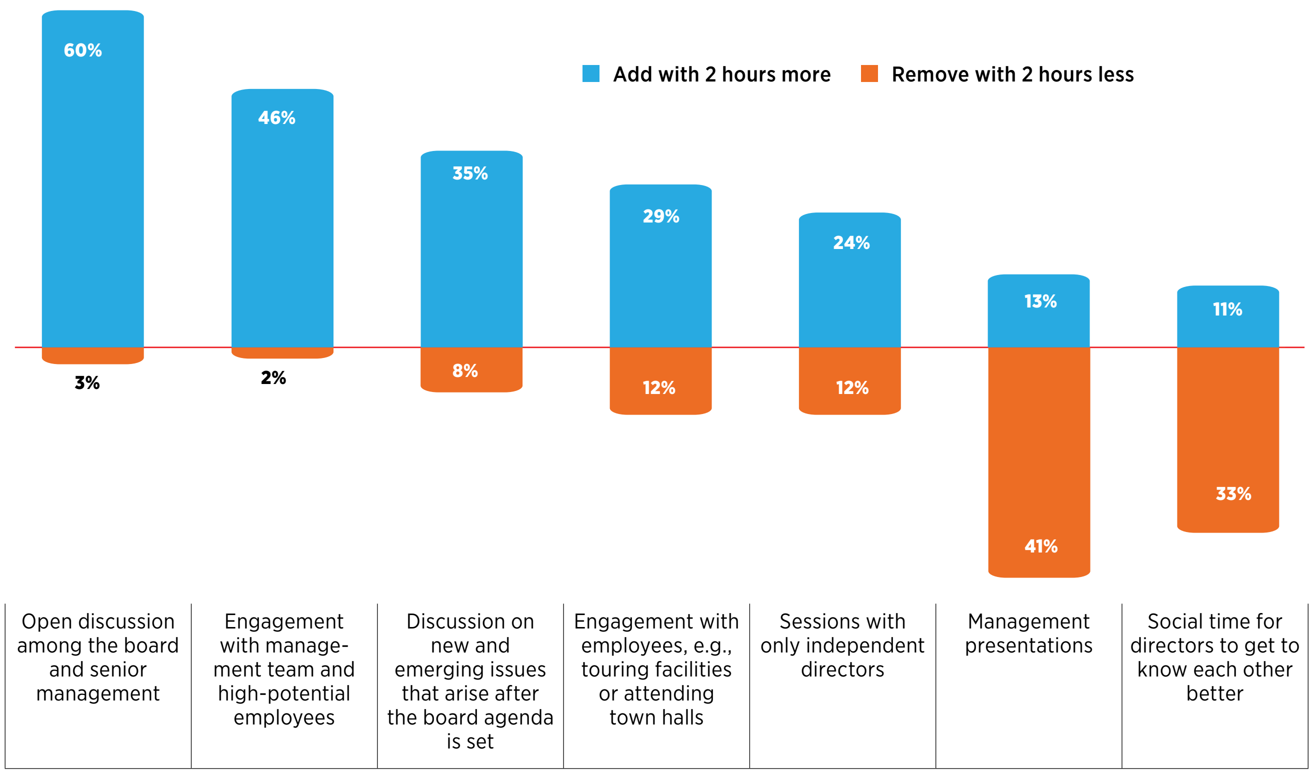
Many seek to reduce management presentation time.

We also asked respondents what they would cut if forced to do their work with two fewer hours. A plurality reported that they would cut back on management presentations (41%). Given other survey responses, one explanation is that many board members seek a dialogue with management rather than passively listening to information that could have been part of pre-meeting board materials. Too much time is spent presenting and focusing on the past rather than action-planning for the future.

Somewhat surprisingly, a third would reduce social time (33%) with directors. This response was consistent for both new and well-seasoned directors and may indicate that board members are either well acquainted with each other and additional social time adds little, or that existing social time should be paired with a business or educational purpose.

When asked where management can improve the quality of information sent to the board, the results were dispersed, suggesting there is no single type of improvement sought. The top three responses were a desire for more interpretation about the importance and meaning of the information presented (33%), improving the ratio of forward-looking information to backward-looking results (33%), and a greater focus on critical key performance indicators (KPIs) (31%). However, when we look at the top three, we see a theme emerge about items that facilitate a discussion rather than ones that simply improve a traditional presentation. One effective approach we have seen is for management to provide executive summaries to each section of board meeting materials highlighting areas of change since previous meetings and calling attention to key points and relevant issues that the board will need to vote on.

What directors would add or remove



Boards have further to go in continuing to evolve the way they work.

One challenge with initiating many of these changes is that creating the right agenda and communicating new expectations with management is difficult—and many directors know it. Many also call out the need for improvement in coming to an agreement with management on both long- and short-term risk-taking, the exact places where more discussion and less presentation would be most helpful. Our survey results reveal a major disconnect in this area that should give board members and CEOs pause: Directors reported high confidence that they are aligned with management on identifying their companies' top risks but express relatively low confidence in alignment with management on both short- and long-term risk appetite.

In a business environment that many board members and corporate leaders describe as one of "permanent uncertainty," this disconnect is a potential red flag that boards may need to address. As has been all too clear in the last several years, internal and external risks can develop and escalate with remarkable speed, and interrelationships between risks can create multiplier effects that greatly increase their negative impact on company operations. On the flip side, companies that invest and seize opportunities in uncertain times can gain significant, lasting competitive advantage. Board members need to prioritize explicit and regular discussions with management about how much risk the firm can and should take on in pursuit of growth and opportunity to survive and thrive.

Survey respondents want to see more forward-looking information and more interpretation from management on meaning. They also seek changes in the way the board operates through more open discussion time, more frequent communications with management outside board meetings, and more meetings with stakeholders and briefings from independent advisors to help the board as a whole come to speed on new and emerging topics. All these changes in the ways boards receive and consume information could help reduce this disconnect and improve board-management alignment on risk appetite.

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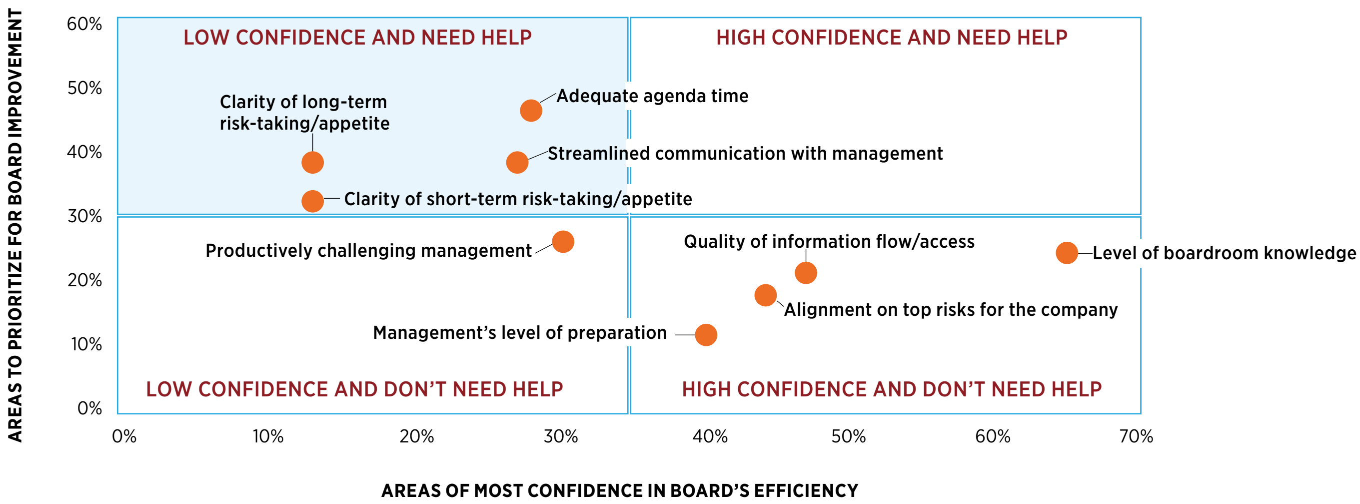
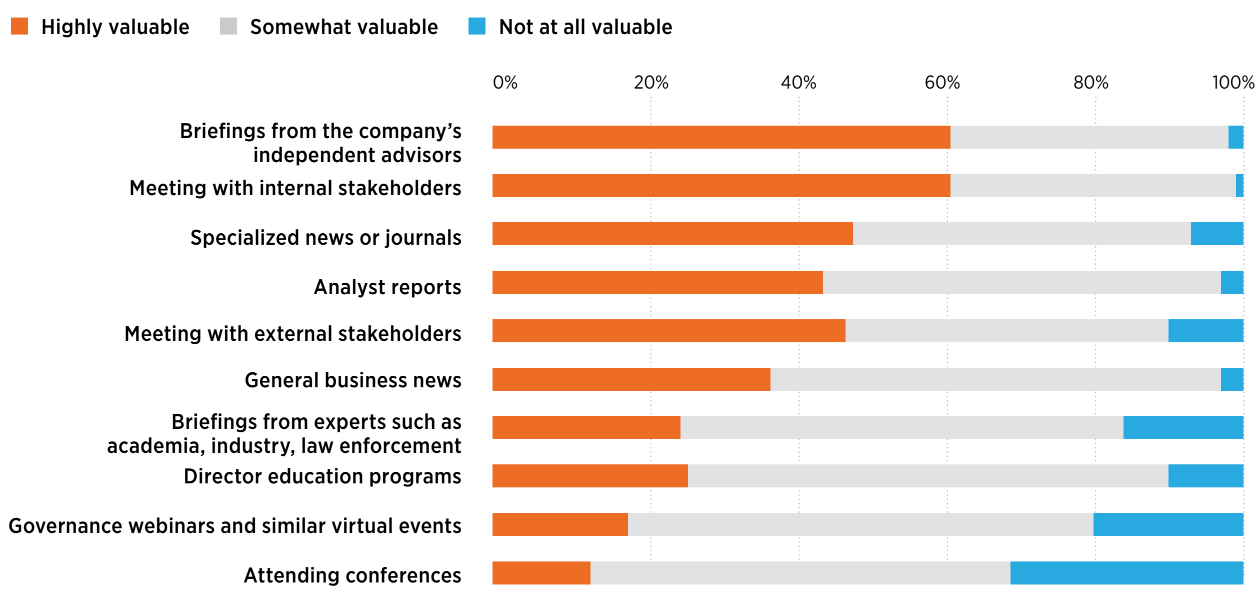
Where boards need help



Value of sources for critical issues in board preparation, selected sources



Directors value both working together and learning together. However, changing the board agenda to add more discussion time may mean that directors will have to spend time outside of the board meeting coming up to speed on critical issues and reviewing routine matters. Interestingly, most directors report that their most valuable interactions are collective experiences, such as meeting with stakeholders or the board's independent advisors. Virtual board meetings and board briefings may be one way to achieve this. For example, a one-hour presentation on an unfamiliar or evolving topic, such as generative AI from the firm's chief information officer (CIO) or emerging consumer trends from an independent advisor, may help to ensure all directors start with a similar set of baseline information, enabling more valuable, and more productive, discussions on emerging technologies or corporate strategy.

THE POTENTIAL POWER OF AI TO TRANSFORM THE BOARDROOM

Generative and other forms of artificial intelligence are as likely to impact the boardroom as they are business models and operations. Looking to the not-too-distant future, generative AI has the power to help board members ask better questions, create more compelling scenarios for tabletop exercises, and streamline board packages and preparation.

MAKING TRADE-OFFS TO EVOLVE THE BOARDROOM

Key board takeaways

• Leading boards recognize that the board of 2030 will likely get work done in a different way than the board of 2020.

• Currently, boards are experimenting with different ways to bring a larger range of topics into the boardroom and expand time for critical discussions.

• Leading boards recognize that intentional trade-offs are necessary to drive continued progress in board effectiveness, including changing the board agenda and asking management for different kinds of information.

To meet current and future obligations, boards must adapt and change how they work. While there is unlikely to be a one-size-fits-all model, there are several common foundational principles from which all boards can build, which are detailed in the EY Board Effectiveness Framework. Though they may increase on the margins, it is unlikely that the number or duration of board and committee meetings will radically increase. The same is likely the case for the time directors commit to their role, which many feel grew in response to the series of disruptions that companies experienced in the past three years. Spending more time in one area likely entails taking time away from other agenda items. Boards may need to make intentional trade-offs as they transform how they receive information and how they get work done. For example, a greater focus on management summaries and KPIs means that the board may have less engagement with corporate performance details. More group learning may mean less collective board time available for other activities or scheduling learning opportunities outside board meetings. Given a wide variety of internal and external pressures, some of these changes may be inevitable.

We have identified a few areas where boards can consider making trade-offs to increase their effectiveness:

Creating more time for discussion in board meetings by doing more work before the board meeting (see next page). For the last two decades, it has been almost conventional wisdom that great boards have great discussions. It is not surprising that board members want more time for dialogue with each other and with members of management. Boards may seek to expand board and committee meeting time to accommodate such discussions. However, in our experience, there is scant evidence of this. Rather, something must come off the agenda. Our survey indicates that many would reduce the time for management presentations. Such presentations often cover routine matters that could be covered in a consent agenda. However, to do this, directors must commit to a careful review of management material as part of board preparation. In short, more time for discussion likely means that board members do more work before the board meeting. They may also need to work with their general counsel and governance teams to put safeguards in place to ensure that all board members can fulfill their fiduciary duties for oversight of routine matters.

WHAT IS A CONSENT AGENDA?

A consent agenda is a part of a meeting agenda, often toward the beginning of a meeting, where the board groups routine matters for collective approval without discussion. This can help reduce the amount of presentation time during the board meeting and can focus meeting time on issues that require substantial discussion. It comes with the expectation that all members of the board or committee have prepared appropriately for the meeting by thoroughly reading all background materials.

Asking management for more interpretation of results while recognizing the potential for a narrow view of the company's position. Some boards have experimented with management giving a written interpretation of financials and other materials in the board book. These can then be the focus of discussion as they specify which topics are for information only, which require specified director dialogue and which require votes or consent. However, boiling down corporate performance to specific mission-critical issues and focusing on a few KPIs that can fit on a dashboard may lead to a more limited representation of the firm's position. This may place a greater burden on management —and the board—to ensure that some safeguards are in place and that an accurate and holistic picture of the firm is in place.

Streamlining board-management communications by coordinating asks from individual directors and working together to prioritize information needs. Management fatigue is real, and many boards see streamlining communications as a means to both clarify expectations and reduce the burden on management. It is not unusual for individual directors to ask well-intended questions of management that may be lower value and consume significant management follow-up time that is out of proportion to the issue's significance for board oversight purposes. A streamlined approach may require individual directors to temper their own requests and take time to coordinate requests with other members of the board. To do so, board leaders (the lead independent director or non-executive chair and key committee chairs) may need to take on more active roles in vetting and coordinating board members' information requests to management.

Principles for making trade-offs

As boards continue to evolve their operating model, it may be useful to keep six principles in mind when considering the necessary trade-offs.

1. Get on the same page—Identify a common understanding of the current state. Take time to educate new directors as to the basic business model, operating model and financials that underline the company. All directors need to stay current with the evolving business environment, key risks and strategic opportunities, and—importantly—ensure that the board and management are aligned on risk appetite.

2. Ensure that there is a shared understanding of the board's current role, the "work to be done" by the board—Gather ongoing feedback via the board evaluation process (see No. 6).

3. Review and assess recent changes in the boardroom—Identify objectives and desires—some of the changes made during COVID-19 may no longer be necessary. Work to ensure that those changes that remain stay for good reason rather than historical inertia.

4. Gain agreement on future changes—Identify additional moves for the board to make and gain collective agreement on the changes. These may be more or less virtual, more discussion or more future-focused, but gain agreement on how the board may evolve.

5. Work with the CEO, corporate secretary and senior management to identify and understand potential trade-offs—Ensure that any critical work is continued in another way. This may include changes to board agendas, board processes or even committee structures. For example, a board with an especially large audit committee agenda may choose to create a separate risk committee.

6. Regularly evaluate board effectiveness with continuous improvement in mind—Reflect on the success (or failure) of the changes, and board/committee performance in general, on a regular basis. In addition to a robust annual board, committee and individual director evaluation process, devote a few minutes at the end of meetings for an informal assessment conversation among directors.

QUESTIONS FOR BOARDS TO CONSIDER

- How is the board intentionally evolving its agenda and time allocation?
- In what ways has the board unintentionally evolved in the past several years? Which of these are important to keep in place?
- What processes and practices are necessary to alter to meet the board's continued objectives?
- What are the impacts on directors, committees and management for making a change?
- What obligations do directors have if a consent agenda is used to approve routine matters? How does the board ensure that all directors do what is necessary to keep a consent agenda?
- If the board were forced to add two hours to the agenda, what would be a top priority?
- What agenda items would be removed or compressed if the board agenda shrunk by two hours?
- Where do discussions on risk appetite appear on board agendas, and how frequently is risk appetite discussed?
- What is the level of alignment between the board and members of management on how much risk the company can and should afford to take on?

SUMMARY

The boardroom has undergone significant change in the last several years, as directors strive to maximize their effectiveness during volatile and uncertain times. Most of these changes are here to stay, but more change is on the horizon. Respondents to our survey continue to seek ways to improve their board's focus on strategic issues to help close the gap that board and management have on critical topics such as risk appetite.

ABOUT THE DATA

In analyzing the data, we considered whether company size or board tenure changed the results. For example, did boards at larger companies have different ways to manage these challenges compared with boards at smaller firms? Did directors new to their board seat respond differently than those with more than 10 years on the board? They did not—answers were consistent across company size and director tenure.

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Effective corporate governance is an important element in building a better working world. The EY Center for Board Matters supports boards, committees and directors in their oversight role by providing content, insights and education to help them address complex boardroom issues. Using the firm's professional competencies, relationships and proprietary corporate governance database, EY teams are able to identify trends and emerging governance issues and then deliver timely and balanced insights, data-rich content, and practical tools and analysis for directors, institutional investors and other governance stakeholders.

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