Corporate Board Practices

IN THE RUSSELL 3000 AND S&P 500 | 2020 EDITION

In collaboration with

ESGAUGE is a data mining and analytics firm uniquely designed for the corporate practitioner and the professional service firm seeking customized information on US public companies. It focuses on disclosure of environmental, social, and governance (ESG) practices such as executive and director compensation, board practices, CEO and NEO profiles, proxy voting and shareholder activism, and CSR/sustainability disclosure. Our clients include business corporations, asset management firms, compensation consultants, law firms, accounting and audit firms, and investment companies. We also partner on research projects with think tanks, academic institutions, and the media.

www.esguage.com

Debevoise & Plimpton LLP is a premier law firm with market-leading practices, a global perspective, and strong New York roots. We deliver effective solutions to our clients' most important legal challenges, applying clear commercial judgment and a distinctively collaborative approach. Our Corporate Governance Practice includes lawyers from each of our Capital Markets, Mergers & Acquisitions, Executive Compensation, Litigation and White Collar Defense teams—all with decades of experience counseling and representing boards and senior managers.

www.debevoise.com

The KPMG Board Leadership Center (BLC) champions outstanding governance to help drive long-term corporate value and enhance investor confidence. Through an array of programs and perspectives—including the KPMG Audit Committee Institute, the WomenCorporateDirectors Foundation, and more—the BLC engages with directors and business leaders to help articulate their challenges and promote continuous improvement of public- and private-company governance. Drawing on insights from KPMG professionals and governance experts worldwide, the BLC delivers practical thought leadership—on risk and strategy, talent and technology, globalization and compliance, financial reporting and audit quality, and more—all through a board lens.

kpmg.com/us/blc

Russell Reynolds Associates is a global leadership advisory and search firm. Our 425+ consultants in 46 offices work with public, private, and nonprofit organizations across all industries and regions. We help our clients build teams of transformational leaders who can meet today's challenges and anticipate the digital, economic, and political trends that are reshaping the global business environment. From helping boards with their structure, culture, and effectiveness to identifying, assessing, and defining the best leadership for organizations, our teams bring their decades of expertise to help clients address their most complex leadership issues.

www.russellreynolds.com

The John L. Weinberg Center for Corporate Governance was established in 2000 at the University of Delaware and is part of the College of Arts & Sciences. It is one of the longest-standing corporate governance centers in academia, and the first and only corporate governance center in the State of Delaware, the legal home for a majority of the nation's public corporations. The Center is recognized as a thought leader in the corporate governance field.

www.weinberg.udel.edu

Corporate Board Practices
in the Russell 3000 and S&P 500
2020 EDITION

by Matteo Tonello

Corporate Board Practices in the Russell 3000 and S&P 500: 2020 Edition documents corporate governance trends and developments at US publicly traded companies—including information on board composition and diversity, the profile and skill sets of directors, and policies on their election, removal, and retirement. The analysis is based on recently filed proxy statements and complemented by the review of organizational documents (including articles of incorporation, bylaws, corporate governance principles, board committee charters, and other corporate policies made available in the Investor Relations section of companies' websites). When relevant, the report highlights practices across business sectors and company size groups.

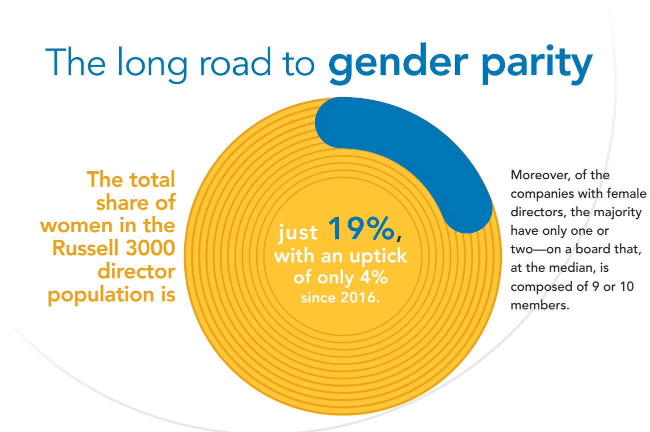
The project is a collaboration among The Conference Board, Debevoise & Plimpton, the KPMG Board Leadership Center (BLC), Russell Reynolds Associates, the John L. Weinberg Center for Corporate Governance at the University of Delaware, and ESG data analytics firm ESGAUGE. See "Access our Online Dashboard" on p. 17 for more information on the study methodology. Visit *conferenceboard.esgauge.org/boardpractices* to access and manipulate our data online.

The following are the key findings and insights.

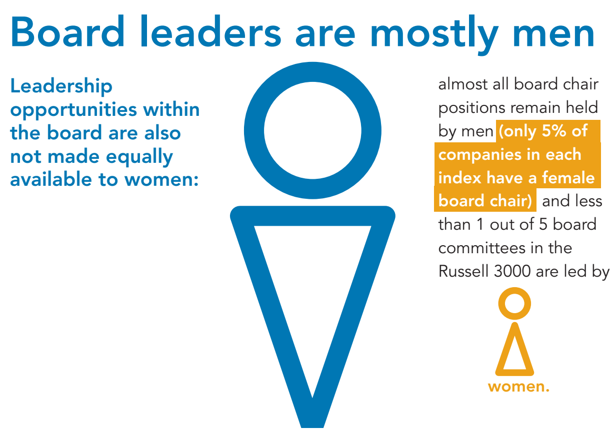
While progress continues to be made, hundreds of US public companies still have an all-male board of directors. Only about 10 percent of S&P 500 companies explicitly disclose individual directors' race (ethnicity), and 8 out of 10 of those board members are white.

Gender diversity has been accelerating, including among smaller companies, but female directors continue to represent less than one-fifth of the total population of board members in the Russell 3000, and 13.4 percent of Russell 3000 companies do not yet have a single woman on their board.

The total share of women in the Russell 3000 director population is just 18.5 percent, an increase of only 4.2 percent since 2016. Moreover, of the companies with female directors, the majority have only one or two—on a board that, at the median, is composed of nine or 10 members. Even in the S&P 500 index, which in 2019 celebrated the election of at least one female director to the last remaining all-male boards, the total percentage of women continues to be shy of one-quarter of all board members. The lowest percentages of female directors are seen in the energy (12.7 percent), health care (17.2 percent), and information technology (17.4 percent) sectors. Energy companies, in particular, report the highest percentage of all-male boards (27.5 percent).



Leadership opportunities within the board are also not made equally available to women: almost all board chair positions remain held by men (only 4.7 percent of companies in each of the Russell 3000 and S&P 500 indexes have a female board chair) and less than 1 out of 5 board committees in the Russell 3000 are led by women.

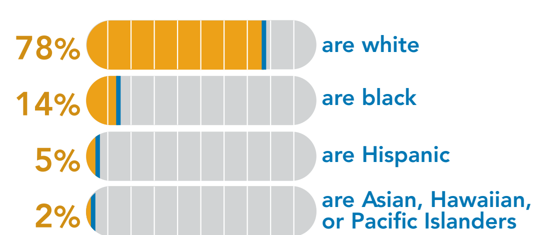


A majority of companies in the S&P 500 include photographs of their directors in proxy statements, which can be an indication of board diversity, particularly in terms of gender. Using photographs to disclose diversity, however, has limitations as it assumes readers will make inferences based on appearance and does not capture the multidimensional nature of diversity. In the S&P 500 index, only 59 companies also disclosed (whether in text or through charts) their individual directors' race (ethnicity), for a total of 658 board members. Companies in the utilities and financials sectors are the most likely to provide this type of disclosure (32.4 percent and 21.1 percent of S&P 500 companies in those sectors, respectively), while only 3.3 percent of consumer discretionary companies offer it. When such disclosure is provided, it is based on self-identification information volunteered by individual directors to the company.

Of those 658 board members whose race (ethnicity) is identified, 8 out of 10 (78 percent) are white, 13.5 percent are black, 5.2 percent are Hispanic, and 2.4 percent are Asian, Hawaiian, or Pacific Islanders (for a total of 22 percent nonwhite). The nonwhite population represents approximately 40 percent of the total population of the United States, according to the US Census Bureau.[1]

Of directors whose race (ethnicity) is identified, 8 out of 10 are white

In the S&P 500, only 59 companies disclose their individual directors' race (ethnicity), for a total of 658 board members. Of these:



What's ahead? The scrutiny of board diversity practices will continue to intensify, driven by multiple factors. More and more institutional investors are following the lead of prominent asset managers such as State Street, Vanguard, and BlackRock, moving diversity to the front and center of their corporate stewardship initiatives.[2] On the eve of the 2020 proxy season, the Office of the New York City Comptroller launched the third phase of its Boardroom Accountability Project, calling out companies that do not have a policy requiring that women and people of color be considered for every open director seat—a version of the so-called Rooney Rule pioneered by the National Football League (NFL).[3] In February 2020, proxy advisor ISS started to implement a new adverse voting recommendation against the chair of the nominating committee of companies with no female board members.[4] In July 2020, a coalition of organizations led by the US Chamber of Commerce sent a letter to the Senate Banking Committee in support of a bill that passed the US House of Representatives last year and would mandate proxy disclosure of self-identified race, ethnicity, and gender of corporate members and executive officers.[5] And, as California has already done, the states of New Jersey, Massachusetts, and Washington have introduced their own legislative proposals setting a female quota for public company boardrooms.[6]

For these reasons, boards should make diversity an integral part of the ongoing board succession planning process. While this is particularly important for those smaller companies where diversity is still lacking, even companies with some board diversity should avoid the risk of being complacent on this important topic and of adopting a check-the-box, compliance approach. The efforts to improve diversity may include: requiring a diverse slate of candidates for each open position; endorsing the model proposed by the Committee for Economic Development of The Conference Board (CED), where every other board seat vacated by a retiring board member is filled by a woman,[7] or the model described in recent California legislation that amended the Corporations Code to require between one and three directors (depending on the size of the board) from an underrepresented community by the end of 2022;[8] ensuring that nominating committees, which take the lead in the director recruitment process, are diverse; and considering diversity when making board and committee leadership appointments.

While the focus in recent years has tended to be on director gender diversity, recent events in the United States and across the world will focus increasing attention on racial and ethnic diversity in the boardroom. Companies should consider getting ahead of investor demands and include more information on the racial and ethnic backgrounds of directors on their websites, even before they issue their next round of proxy statements, as part of a broader explanation of the multiple dimensions of board diversity. In considering and disclosing diversity, companies should not feel constrained by EEOC reporting categories on race,[9] which are limited and may not reflect the full ethnic diversity of the board.

Insights for What's Ahead

When the COVID-19 pandemic hit, most US corporate boards demonstrated their responsiveness and resilience by increasing their number of meetings, the frequency of their communication with management, and their focus on key areas such as their liquidity, workforce, and operations.[a] The combination of crises confronting companies today, however, has raised the bar even higher for boards: it has not only increased the list of items on board agendas, but also brought greater attention to a range of corporate board practices—including issues such as gender and racial diversity in boardrooms.

This report provides an analysis of recent trends in corporate board practices, as well as actionable insights for boards seeking to adjust their board composition and practices to face the challenges ahead.

- In promoting diversity of board composition, companies should not simply seek to satisfy numerical targets set by certain investors or proxy advisory firms. Instead, they should make diversity an integral and ongoing part of their director searches—as well as consider diversity in choosing the members of their nominating and other committees. Companies should also get ahead of the curve to increase their disclosure on the diversity of their boards by providing narrative information about the background of their board members.
- Companies can advance the gender, age, racial, ethnic, and cognitive diversity of their boards by looking outside the C-suite and to those who have not served as public company directors before. To help ensure that these newly minted directors have the requisite experience and abilities to serve as strong all-around directors, boards should put in place robust processes for identifying, recruiting, onboarding, and engaging directors to help them succeed. Boards should also examine their own culture to ensure that incumbent directors and management are providing a genuinely inclusive environment.
- Boards will increasingly benefit from having a combination of long-serving directors, those who bring fresh skills and perspectives, and those in the middle. They should consider how best to achieve that mixture of tenures, disclose that range of tenures to investors, and consider adopting average tenure and similar policies that encourage a healthy level of turnover but avoid the shortfalls of rigid term limits.
- With the time commitment required by public company board service increasing, boards should take a fresh look at their policies and practices governing the number of other public company boards on which their CEO and other directors can serve. Boards should also take a close look at individual directors' ability to commit the time necessary to their roles, as part of the annual board self-evaluation, nomination, and committee appointments processes.

Corporate boards are now at an inflection point. As we entered 2020, boards were facing expanded responsibilities, increased workloads, and greater scrutiny of their composition. That has only increased with the current health, economic, and social crises stemming from the COVID-19 pandemic and the increased focus on race and social injustice. Companies are also on the threshold of generational change in the boardroom, as a large cohort of directors is nearing retirement age.

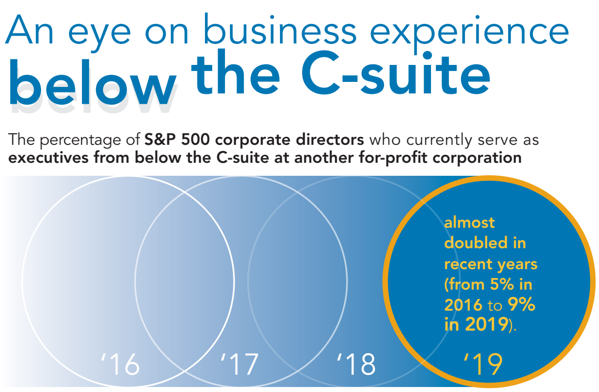
Boards have a window of opportunity to embrace changes in their composition and practices that align with their companies' strategies and meet new investor demands, in a way and at a pace that makes sense for the company based on its individual circumstances.

[a] "Governance in a Time of Crisis: Preparing Your Board for the Challenges Ahead," *ESG Watch*, The Conference Board, July 13, 2020. Also see Rusty O'Kelley, Paul Rodel, Matteo Tonello, and Paul Washington, *Corporate Governance Challenges in the COVID-19 Crisis. Findings from a Survey of US Public Companies*, The Conference Board, June 2020.

With new skill sets now in demand, companies are increasingly looking for directors beyond the C-suite. However, they remain cautious of nominees without prior board experience.

Prior C-suite experience continues to be prevalent among public company boards. About 3 out of 10 Russell 3000 board members have CEO-level experience at for-profit companies. Another third of board members are either active or former C-suite executives at another for-profit company. But the percentage of S&P 500 corporate directors who currently serve as executives from below the C-suite at another for-profit corporation almost doubled in the last three years (from 4.7 percent in 2016 to 8.9 percent in 2019) and has risen from 8 percent to 11.6 percent in the Russell 3000.

The highest percentages of Russell 3000 board members who are active executives from below the C-suite at another for-profit corporation are seen in the communication services (14.7 percent, up from 11 percent in 2016), health care (13.5 percent, up from 9.8 percent), and information technology sectors (13.2 percent, up from 8.4 percent). By contrast, the sectors with the lowest percentages of directors with these qualifications are utilities (7.9 percent, up from 3.7 percent in 2016) and financials (9.9 percent, up from 7.3 percent).



With regard to specialized skill sets, finance and information technology are the most frequently mentioned: 13.8 percent of board members in the Russell 3000 (up from 10.9 percent in 2016) report having some type of technology background, while 21.7 percent are identified as an "audit committee financial expert," as per SEC disclosure rules. In the S&P 500 index of larger companies, 20.9 percent of corporate directors include technology expertise in their biographical profile. IT companies have, by far, the highest percentages of board members with a technology background (40.3 percent of all Russell 3000 directors at companies in the sector), followed by communication services firms (18.7 percent). Organizations in the materials, consumer staples, and industrials industries attract the largest share of directors with international expertise (14.7, 13.2, and 11.4 percent, respectively). Financials (3.8 percent), real estate (3.8 percent), and utilities (3.7 percent) sectors are on the opposite end of the spectrum for directors with an international background.

Prior for-profit company board experience continues to be widely prevalent among public company boards for newly elected directors. In both the Russell 3000 and S&P 500 indexes, about three-quarters of companies reported electing no first-time director (i.e., an individual who has never served before as a public company director) in the 2019 disclosure year, a percentage almost identical to the one from 2016. In the S&P 500, about 1 out of 5 companies elected one first-time director to their board, while only 2.6 percent elected two. In the Russell 3000, the percentages of companies electing one and two first-time directors are 18.9 and 3.2 percent, respectively.

Technology

expertise is in demand

14% of board members in the Russell 3000 (up from 11% in 2016) report having some type of technology background.

IT companies have, by far, the highest percentage of such directors (40%), followed by communication services firms (19%).

What's ahead? As companies face new strategic challenges, changed expectations from the labor force, and rapidly evolving consumer interests, the scope of board and committee responsibilities will continue to expand. For example, research shows that board committee charters, in particular, are being revised to accommodate a new array of oversight responsibilities—from cybersecurity to digital transformation, and from climate change risk to human capital management.[10]

First-time director?

Let us **think** about it

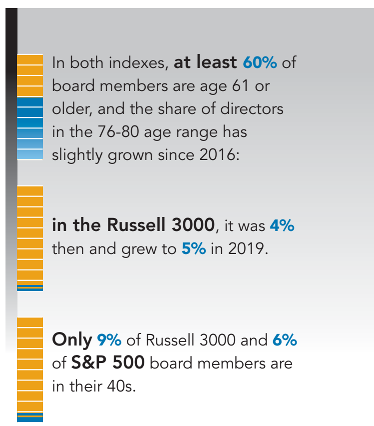
In both indexes, about 3/4 of companies reported electing no first-time director (i.e., an individual who has never served before as a public company director) in the 2019 disclosure year, a percentage almost identical to the one from 2016.

Along with those expanding responsibilities comes the need for a diversity of skills, perspectives, and problem-solving approaches. As companies seek individuals with specific skill sets, they should consider professionals who have not served on corporate boards before or who do not have C-suite experience. As a result, they will benefit from more robust processes for identifying, recruiting, onboarding, and engaging corporate directors—including tailored onboarding programs to help ensure that these new directors are prepared to participate in board deliberations along with their more seasoned peers. Companies that do not yet do so should also consider adopting the skills matrix model of disclosure of director qualifications and skills: in addition to enhancing transparency to investors and other stakeholders, it provides for a valuable strategic and board assessment exercise.

The average age of directors in both the Russell 3000 and S&P 500 remains unchanged, while the share of board members age 70 or older has in fact increased in the last few years.

The average age of directors is 63.4 in the S&P 500 and 62.6 in the Russell 3000, with no appreciable change over the last few years. In both indexes, at least 60 percent of board members are age 61 or older, and the share of directors in the 76–80 age range has slightly grown since 2016 (in the Russell 3000, it was 4.2 percent then, and it grew to 5 percent in 2019). Overall, the data suggest that companies continue to remain skeptical of the contribution that professionals under the age of 50 can make as directors: only 8.5 percent of Russell 3000 board members are in their 40s, and the percentage in the S&P 500 is even lower (5.6 percent).

Companies continue to remain skeptical of the contribution that **directors under age 50 can make**



Younger directors are more frequently found on smaller companies' boards. For example, the percentage of directors age 46–50 among Russell 3000 companies with annual revenue under $100 million (9 percent, up from 10.1 percent in 2018) is more than twice as high as the one for the largest size group of annual revenue of $50 billion and over (3.8 percent). The real estate sector shows the highest percentage of board members in the 76–80 age range (7.5 percent), while the highest percentages of board members who are 45 or younger are found in the energy (7 percent) and communication services sectors (6.6 percent).

While mandatory director retirement policies based on age are often disclosed as a feature of the board succession planning process (we found them at 69.8 percent of S&P 500 companies and 39.3 percent of Russell 3000 companies), many companies choose to formally authorize the board to make exceptions to their enforcement. Most institutional investors are agnostic about the topic of mandatory retirement ages: some view it as an overly rigid, one-size-fits-all solution, while others are concerned that a retirement policy based on age may raise discrimination issues.[11] To be sure, the strict version of this policy, which does not allow exceptions, is found at only 21.6 percent of Russell 3000 companies and 36.7 percent of S&P 500 companies. When this type of policy is used, the retirement age is typically set at 72 years (35.1 percent of the Russell 3000 cases with a policy in place) or 75 years (44.2 percent).

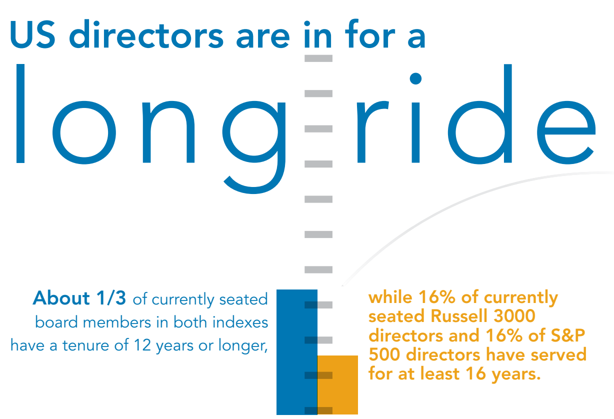
What's ahead? In the coming years, due to an impending generational turnover and the search for a broader set of director skills, the average age of board members is likely to begin to decline. As mentioned above, top leadership talent in areas such as digital transformation, cybersecurity, human capital management, and sustainability is in high demand and will likely drive the appointment of younger professionals to corporate boards. Furthermore, as the debate on inclusiveness intensifies, age may increasingly become an additional metric to assess board diversity.

Amid shifting consumer interests and the challenges of a rapidly changing business environment, boards should consider having an informed discussion of age diversity in their leadership and ensure they are positioned to attract the best individuals to these roles. A retirement policy based on director age may support the board succession process in situations where a company concludes that, for strategic reasons, board refreshment should be accelerated. However, while the attention to age diversity should increase, it is equally important for companies to have board members with sufficient professional and life experience to effectively perform in the director capacity. In recruiting younger directors, it will be important for boards to consider whether the prospective board members have had failures as well as successes; have held a number of different professional positions over time, each with its own set of challenges; and have developed the ability to be focused outward rather than on personal career advancement.

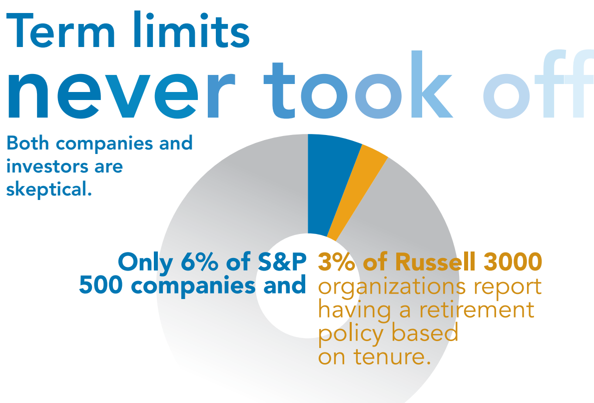
While boards of directors have a mix of tenures, US directors continue to serve longer than those in other jurisdictions: the average US board has at least two members who have served for 12 years or longer.

US public company directors are in for a long ride: average tenure for seated directors is 9.7 years in the larger companies of the S&P 500 index and only slightly lower (9.5 years) among the broader Russell 3000 index. By way of comparison, the average tenure of directors at the largest companies in the United Kingdom's FTSE index is 4.1 years.[12] The data also show that 21.6 percent of Russell 3000 departing directors had served on the board for more than 15 years before stepping down in 2019, and the percentage rises to 26.3 in the S&P 500.

The analysis for both indexes shows a wide mix of tenures on the average board of directors. However, about one-third of currently seated board members have a tenure of 12 years or longer, while 15.9 percent of currently seated Russell 3000 directors and 16.2 of S&P 500 directors have served for at least 16 years.



The longest median tenures of departing board members are seen in the financials (10.7 years) and utilities (10.5 years) sectors. The shortest median tenures are in the health care (6.2 years) and energy (7.4 years) business sectors. While there is no clear correlation between departing director tenure and company size, our data show that, in general, small-company directors serve for shorter periods of time: the group of manufacturing and nonfinancial services companies with less than $100 million in annual revenue has by far the highest percentage of firms with an average departing director tenure of less than six years (slightly more than half of the subsample, or 53.2 percent, compared to 23.4 percent of those with annual revenue of $50 billion or higher) and the lowest percentage of firms with an average departing director tenure of more than 15 years (10.0 percent, compared to 21.9 percent of those with annual revenue of $50 billion or higher). These differences explain the discrepancies observed in the index analysis between the S&P 500 and Russell 3000 indexes.



Term limits, or mandatory retirement policies based on tenure, continue to remain uncommon as companies prefer having the flexibility to retain valuable board members despite their long service. Only 5.6 percent of S&P 500 companies and 3.3 percent of Russell 3000 organizations report having such a policy.

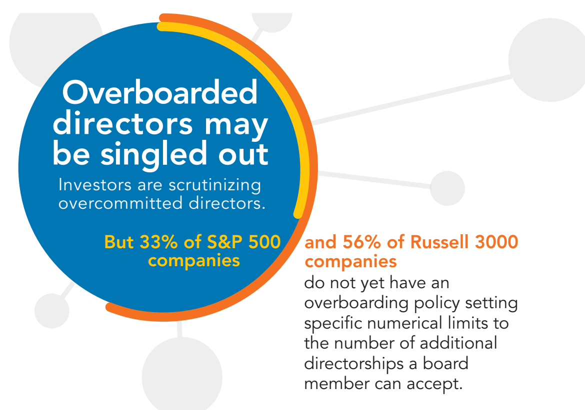
What's ahead? Average director tenure and the mix of tenures on the board are increasingly disclosed in proxy statements and have become frequent topics of engagement with institutional investors. This is especially true in situations where longer-serving directors are an impediment to the efforts to adjust the strategic course, improve demographic diversity, and add to the boardroom a broader set of strategic competencies and professional backgrounds.

Companies should monitor and consider disclosing tenure metrics. Unless a specific circumstance warrants it, however, the solution to a director tenure issue is unlikely to be found in the use of term limits. Most institutional shareholders and proxy advisors are skeptical about them and view them as an overly rigid, one-size-fits-all mechanism that short-circuits the director election process and may arbitrarily force experienced and knowledgeable directors off the board.[13] Instead, companies should consider strengthening their routine director evaluation process to ensure that specific cases of long tenures are examined holistically and in light of other assessment factors—including the overall gender, age, racial and ethnic diversity, diversification of skills, and rate of refreshment of the board.

In general, a board composition assessment process should be more mindful of the mix of tenures than of rigid tenure limits. By mixing different tenures, boards can in fact optimize knowledge continuity without compromising independence. In addition, the ideal board includes the right combination of directors who have contributed to the choice of the incumbent CEO and directors elected after the CEO's appointment.[14] In situations where the average tenure does appear too high, companies can consider average tenure policies that allow for a mix of tenures but also provide a mechanism to ensure that, as a board reaches the limit, it considers either the departure of longer-serving directors or the addition of new members. Perhaps most importantly, high average tenure can prompt a discussion about the fact that a successful director does not have to be a long-tenured director. This discussion would help the board's culture to evolve and help individual directors to appreciate the importance of a reasonable rate of turnover.

At least one-fifth of S&P 500 companies and one-third of Russell 3000 companies do not comply with key investor voting guidelines on director overboarding, and a large majority of companies in both indexes do not specifically restrict the additional board services of their CEO.

A little more than a decade ago, so-called director overboarding policies were found in only a minority of companies. Times have changed, and the ever-expanding responsibilities of board service have prompted many companies to formally regulate the number of additional for-profit directorships their board members can accept. According to the review of 2019 disclosure documents, overboarding policies setting specific numerical limits are found at 66.7 percent of S&P 500 companies (up from 64.4 percent in 2016) and 43.9 percent of Russell 3000 companies (up from 43.2 percent). As much as 61.3 percent of Russell 3000 companies in the utilities business do have an overboarding policy, while the policy is reported by only 31.9 percent of health care companies and 38.8 percent of financial services companies.



The data also show a direct correlation with the size of the company: restrictions on the number of directorships are in effect at 80.4 percent of companies with annual revenue of $50 billion or higher, but the percentage declines steadily as the size of the company decreases and is down to only 15 percent among companies with annual revenue under $100 million. Most director overboarding policies set a limit of up to three or four other for-profit company boards (34.4 percent and 45.4 percent of Russell 3000 companies with such a policy, respectively).

But the data also show that 34.7 percent of the Russell 3000 policies either are silent on the subject of overboarding or acknowledge the need for restrictions on other directorships but choose to defer to a case-by-case determination of the nominating/governance committee of the board rather than setting a specific maximum number of other board seats.[15] Some of the policies that provide for the discretionary evaluation of specific circumstances may include the expectation for directors to notify the nominating committee before accepting a new directorship, but these policies seldom prescribe a preapproval requirement. In other cases, they may set specific restrictions that apply to audit committee members (given the additional restrictions in stock exchange listing standards regarding those committees) but not to all directors.

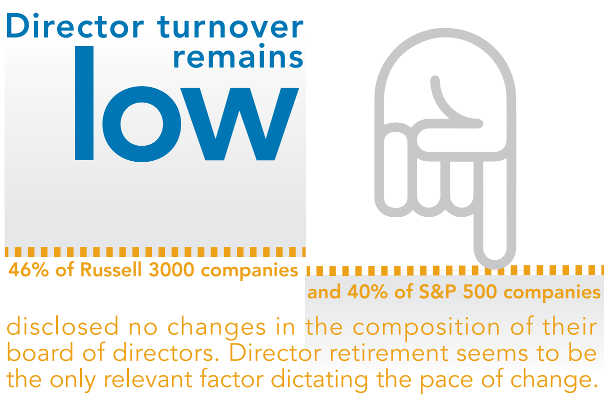
Finally, our research found that a minority of companies use more stringent overboarding rules for their own CEO than for other board directors. In the S&P 500, only 23.8 percent of companies have a specific policy preventing the overboarding of their chief executive, compared to 17.1 percent of the Russell 3000. When these separate provisions are in place, they almost always limit the number of additional board seats to two (56.4 percent of cases in the Russell 3000) or one (40.7 percent). Some 21.1 percent of CEO overboarding policies used by utilities firms (by far the highest percentage across business sectors) permit the CEO to serve on as many as three other boards of directors.

What's ahead? Director overboarding has been a concern to many shareholding institutions and proxy advisors for some time, but in the last year alone the pressure on companies to regulate the matter has intensified. The unprecedented number of Russell 3000 directors receiving less than 70 percent and even 50 percent support levels reported by The Conference Board in its last postseason report was widely attributed to vote-against campaigns prompted by issues of board composition and overboarding.[16] In April 2019, in particular, Vanguard updated its proxy voting guidelines for US portfolio companies, announcing that it would vote against any public company CEO or other named executive officers serving on more than one outside board and any nonexecutive director serving on more than four other public company boards.[17] These guidelines for CEOs track those already in effect at BlackRock, which is even more stringent, limiting the maximum number of additional public company boards to three, not four.[18]

The focus on overboarding is expected to increase, especially as directors' responsibilities are complex, time consuming, and likely to continue to expand in these times of crisis.[19] To avoid adverse votes or other reputational repercussions, companies should familiarize themselves with the thresholds set by major institutions and proxy voting advisory firms, and take a fresh look at their policies and practices in this area. Even more importantly, to help ensure that all board members have the time to devote to their responsibilities, boards should consider the bandwidth of individual directors as part of their nomination, annual performance evaluation, and committee assignment processes. Furthermore, companies should consider proactively engaging with large investors on potential or recent overboarding concerns—a task that may be best filled by an independent board chair, lead independent director, or chair of the nominating and governance committee.

Director turnover remains low. Almost half of Russell 3000 companies and 40 percent of S&P 500 companies made no changes to the makeup of their board of directors last year.

The study examined data on board seats replaced during the disclosure year and directors otherwise added to the board (whether to fill a new seat or to replace a director who had vacated a seat in a previous year). According to the index analysis, 46.2 percent of Russell 3000 companies and 40.1 percent of S&P 500 companies disclosed no changes in the composition of their board of directors. Director retirement seems to be the only relevant factor dictating the pace of change, as these figures are substantially comparable to those recorded in recent years, and data on director age and tenure have also remained remarkably stable.



About one-third of companies in both indexes added a new director or replaced one board seat in the previous 12 months, whereas 19 percent of S&P 500 companies and 15.1 percent of Russell 3000 companies added two new directors. Only 8.6 percent of companies in the Russell 3000 had three or more new incoming directors. The communication services and energy sectors reported the highest shares of companies with turnover of more than five board seats across the 11 GICS groups (3.5 and 4.6 percent, respectively). The real estate and industrials groups of industries reported the highest percentages of companies with no newly elected board member (52.3 percent and 51 percent, respectively).

However infrequent, board changes are more likely to be seen among larger organizations. While on average 9.1 percent of Russell 3000 companies with less than $1 billion in annual revenue disclosed three or more newly appointed directors in 2019 filings, among companies with revenue of $25 billion or higher the average percentage rises to 14.8. Of the smallest financial and real estate companies, with asset value under $500 million, the share that reported no director turnover in the previous year is 57.9 percent, or almost twice as high as the one found in the largest group, with asset value of $100 billion or higher (31.1 percent).

What's ahead? Board succession planning is taking on greater significance amid increasing demand for gender, racial, and ethnic diversity; the strategic diversification of skill sets and professional backgrounds; and more stringent oversight of overboarding. Moreover, considering that about 40 percent of Russell 3000 directors are age 66 or older and almost 30 percent have been on the job for more than 12 years, in the near future a generational change may compound the effects of other driving factors of board refreshment.

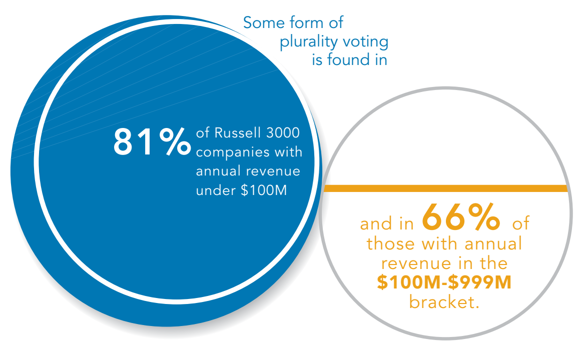
The board of directors is a critical asset to a public company. While refreshment of board composition is important, it should not work to the detriment of the key strategic contribution that individual board members may offer—irrespective of their age or the length of their affiliation with the corporation.

As much as the attention to board composition has intensified, institutional investors and proxy advisors recognize that, ultimately, no preset rule should preempt the judgment of directors. Instead, the solution is a sound board succession plan and a rigorous director evaluation process, which should be explicitly tied to the company's strategic objectives. A consensus on turnover can help inform discussions on all of the topics discussed elsewhere in this report, including board diversity, tenure, and overboarding. And it is important to ensure that the consensus is reflected in board culture so that it is in fact put into effect.

Almost half of Russell 3000 companies continue to use some form of plurality voting to elect their directors and to retain classified board structures where directors do not face annual elections.

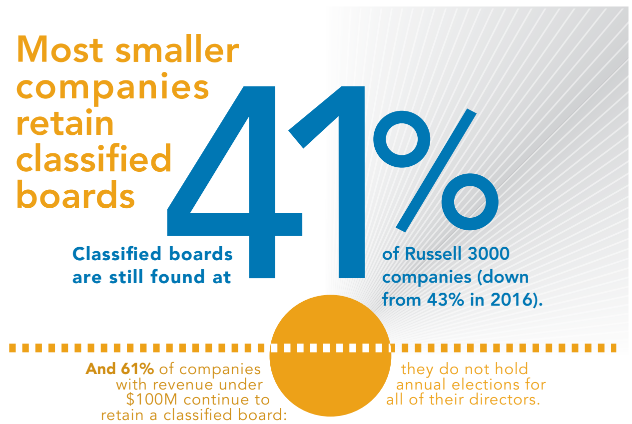
Voting standards for director elections differ greatly depending on the size of the company. Though declining in popularity, a simple plurality voting standard remains widely used among smaller companies. Under the simple plurality voting standard, which operates by default under Delaware law unless the company opts otherwise through its charter or bylaws, uncontested nominees who receive the most "for" votes are elected to the board until all board seats are filled, even if a majority of shares are voted against those individuals. A slight variation is the "plurality plus" standard, under which directors who received more "withhold" votes than "for" votes must formally tender their resignation to the board. In 2019, 40.9 percent of Russell 3000 companies still had a simple plurality voting system (down from 45.5 percent in 2016), while 8.5 percent opted for the "plurality plus" variant (slightly up from 7.9 percent in 2016). Some form of plurality voting is found in 81.3 percent of Russell 3000 companies with annual revenue under $100 million and in 66.3 percent of those with annual revenue in the $100 million–$999 million bracket. By way of comparison, in the S&P 500, only 9.6 percent of companies still use either the simple plurality standard or the "plurality plus" standard.

Plurality voting is far from gone



Findings on board classification are also highly dependent on company size. Our data show that a majority of companies in both indexes now elect members of their boards of directors annually, having abandoned the staggered-years structure of the past.[20]

However, classified boards are still found at 41.2 percent of Russell 3000 companies (down from 43.2 percent in 2016) and 10.9 percent of S&P 500 companies (down from 15.4 percent in 2016). Director classes continue to be used by 57.5 percent of health care companies and 46.1 percent of information technology companies, while less than one-fifth of real estate firms still retain them. The company size analysis, however, is the most revealing, with striking differences between small and larger organizations. For example, only 6.7 percent of financial institutions with asset value of $100 billion or higher have classified boards (it was 9.3 percent in 2016), compared to 43.6 percent of those with asset value between $500 million and $999 million. And 61.3 percent of companies with revenue under $100 million continue to retain a classified board and do not hold annual elections for all of their directors.



What's ahead? Directors and executives should be aware that some investors are now specifically targeting governance issues at smaller firms. While some organizations in that cohort have thus far remained immune to changes in their director election system, things may change. After years of decline, the volume of shareholder resolutions on majority voting has started to rise again, as institutional shareholders are shifting their attention to the smaller public companies outside of the S&P 500. Ending a few years of hiatus, in 2019 CalPERS resumed its push for smaller Russell 3000 companies to also change their director election model to majority voting.[21] Research shows that companies that have recently adopted majority voting are benefiting from the decision as their director nominees are less likely to receive a "withhold" vote of 30 percent or above than they were under the plurality voting model.[22]

Directors, especially at smaller companies, should take a careful and holistic look at changing their director election practices. While plurality voting and staggered boards can be seen as protections against activism, as mentioned above they can also invite activism. Staggered boards can also serve as an impediment to board refreshment, and companies may wish to consider shifting to annual elections if it helps them adjust the composition of the board in a way that keeps pace with strategic needs.

Access our Online Dashboard

Corporate Board Practices in the Russell 3000 and S&P 500: 2020 Edition documents corporate governance trends and developments at 2,826 companies registered with the US Securities and Exchange Commission (SEC) that filed their proxy statement in the January 1 to December 31, 2019 period and, as of January 2020, were included in the Russell 3000 Index. For comparative purposes, the study also includes 496 companies in the S&P 500 Index. The proxy statement analysis is complemented by the review of organizational documents (including articles of incorporation, bylaws, corporate governance principles, board committee charters, and other corporate policies made available in the Investor Relations section of companies' websites).

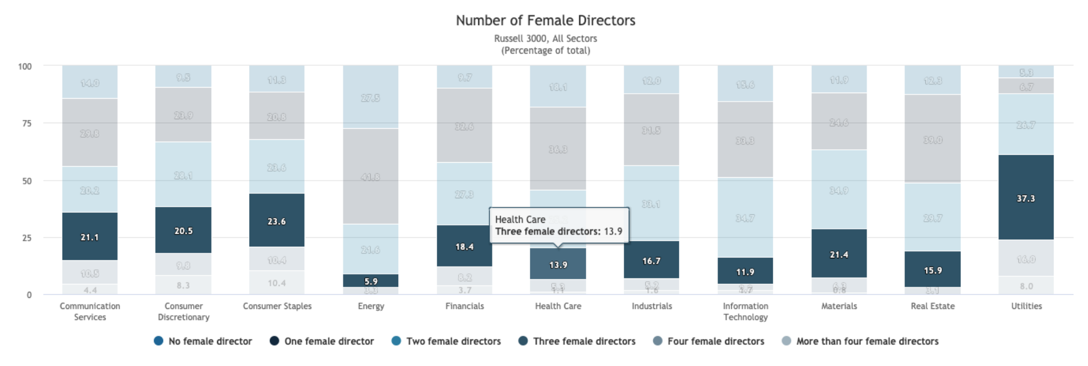
Data from *Corporate Board Practices in the Russell 3000 and S&P 500: 2020 Edition* can be accessed and visualized through an *interactive online dashboard*. The dashboard is organized in four parts:

Part I: Board Organization provides benchmarking information on the size of the board and the frequency of its meetings, its leadership and the safeguards adopted to ensure leadership independence, the board committee structure, and the process for the assessment of the performance of director responsibilities (at the board, committee, and individual director level).

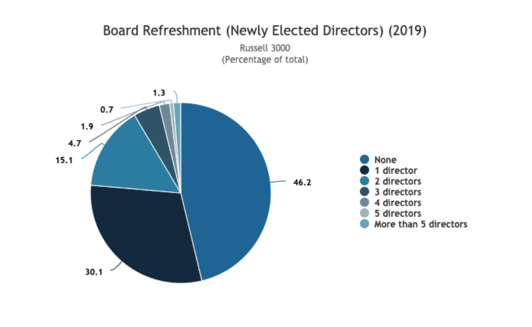
Part II: Director Profile reviews the demographics of the director population (their age, gender, tenure, and qualifications and skills), director independence and existing affiliations with the company or its employees, as well the directorships they currently hold at other for-profit and not-for-profit organizations.

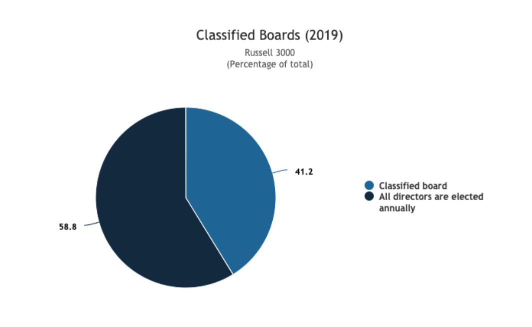
Part III: Director Election and Removal examines voting standards adopted for the nomination and election of board members (whether majority voting, plurality voting, or variations of the same), the process followed to fill newly created board seats, and existing policies for the removal of directors for cause. A section of Part III is dedicated to a comprehensive analysis of companies that have introduced proxy access bylaws, including: the share of ownership and the holding period required by nominating shareholders; the percentage of board seats eligible for proxy access nominations; and special provisions such as those on the maximum number of aggregated shareholders, on related entities, and on loaned shares.

Part IV: Other Board Policies illustrates data on mandatory director retirement policies (based on age and tenure) and on the resignation of directors for change of employment status or the termination of the CEO employment relation. A section of Part IV reviews so-called overboarding policies, including the requirements to notify the board and seek preapproval of new directorships for which board members have received an offer from another company. Additional board practices described in Part IV include: the adoption of policies to promote board diversity; whether the company publishes a matrix to illustrate its directors' qualifications and areas of expertise; the indemnification and the limitation of board members' personal liability; whether directors are eligible for matching gifts programs offered to employees; and how companies support their board members' need for orientation and continuing education.



Data on board practices are segmented according to the business sector and the size of companies. The industry analysis aggregates companies within 11 groups (Exhibits 2 and 3), using the applicable Global Industry Classification Standard (GICS). For the company-size breakdown, data are categorized along seven annual-revenue groups (based on data received from manufacturing and nonfinancial services companies) and seven asset-value groups (based on data reported by financial services and real estate companies, which tend to use this type of benchmarking criteria). Annual revenue and asset values are measured in US dollars (Exhibit 4).





Comparisons with the S&P 500—another commonly followed equity index—are also included to offer an additional perspective on the difference between large and small firms (Exhibit 1). However, figures and illustrations refer to the Russell 3000 analysis unless otherwise specified.

Access the dashboard at:
conferenceboard.esgauge.org/boardpractices

Exhibit 1—Sample Distribution, by Index

Index	n=
Russell 3000	2826
S&P 500	496

Source: ESGAUGE, 2020.

Exhibit 2—Sample Distribution, by Business Sector

Business Sector (GICS)	n=	Percent of total
Communication Services	114	4.0%
Consumer Discretionary	327	11.6%
Consumer Staples	106	3.8%
Energy	153	5.4%
Financials	534	18.9%
Health Care	452	16.0%
Industrials	384	13.6%
Information Technology	360	12.7%
Materials	126	4.5%
Real Estate	195	6.9%
Utilities	75	2.7%

Source: ESGAUGE, 2020.

Exhibit 3—Business Sectors, Industry Groups, and GICS Codes

Business Sector	GICS Code	Industry Group	GICS Subcode
Communication Services	50	Media & Entertainment	5020
	50	Media & Entertainment	5020
	50	Telecommunication Services	5010
Consumer Discretionary	25	Automobiles & Components	2510
	25	Consumer Durables & Apparel	2520
	25	Consumer Services	2530
	25	Retailing	2550
Consumer Staples	30	Food & Staples Retailing	3010
	30	Food Beverage & Tobacco	3020
	30	Household & Personal Products	3030
Energy	10	Energy	1010
Financials	40	Banks	4010
	40	Diversified Financials	4020
	40	Insurance	4030
Health Care	35	Health Care Equipment & Services	3510
	35	Pharmaceuticals, Biotechnology & Life Sciences	3520
Industrials	20	Capital Goods	2010
	20	Commercial & Professional Services	2020
	20	Transportation	2030
Information Technology	45	Semiconductors & Semiconductor Equipment	4530
	45	Software & Services	4510
	45	Technology Hardware & Equipment	4520
Materials	15	Materials	1510
Real Estate	60	Real Estate	6010
Utilities	55	Utilities	5510

Source: MSCI Inc., 2020.

Exhibit 4—Sample Distribution, by Company Size

Annual Revenue		
(All companies except Financials and Real Estate)	**n=**	**Percent of total**
Under $100 million	253	9.0%
$100 million-999 million	672	23.8%
$1 billion-4.9 billion	718	25.4%
$5 billion-9.9 billion	187	6.6%
$10 billion-24.9 billion	172	6.1%
$25 billion-49.9 billion	44	1.6%
$50 billion and over	51	1.8%

Source: ESGAUGE, 2020.

Asset Value		
(Financials and Real Estate companies)	**n=**	**Percent of total**
Under $500 million	19	0.7%
$500 million-999 million	39	1.4%
$1 billion-9.9 billion	439	15.5%
$10 billion-24.9 billion	110	3.9%
$25 billion-49.9 billion	55	1.9%
$50 billion-99.9 billion	22	0.8%
$100 billion and over	45	1.6%

Source: ESGAUGE, 2020.

Unless otherwise specified, figures included in the tables and charts of the report refer to median (midpoint) values. Where appropriate, to highlight possible outliers, the report may also reference the mean (average) of observations.

Data and analysis included in this report are descriptive, not prescriptive, and should be used only to identify the latest practices and emerging trends. None of the commentaries included are intended as recommendations on board structure or other governance practices. The Conference Board, Debevoise & Plimpton, Russell Reynolds Associates, the John L. Weinberg Center for Corporate Governance at the University of Delaware, and ESGAUGE recommend that board policies be adopted after careful consideration of the specific circumstances the company faces in the current marketplace, including its strategic priorities and investor relations.

Access the dashboard at: *conferenceboard.esgauge.org/boardpractices*

Online Dashboard Table of Contents

Visit: *conferenceboard.esgauge.com/boardpractices*

Endnotes

1 *QuickFacts—United States*, United States Census Bureau, last updated in April 2019.

2 BlackRock, for example, issued an extensive statement elaborating on board diversity as an investment issue and, in its annual Stewardship guidelines, encourages portfolio companies to expand on the disclosure of their approach to diversity by including details on how diversity is taken into account not only in the director nomination process but also in board performance evaluations. See *Investment Stewardship's Approach to Engagement on Board Diversity*, BlackRock, January 2020, and *BlackRock Investment Stewardship. Corporate Governance and Proxy Voting Guidelines for U.S. Securities*, BlackRock, January 2020, p. 5.

3 To launch the initiative, NYC Comptroller Scott Stringer sent a letter to 56 S&P 500 CEOs without a Rooney Rule policy, regardless of the current diversity of their boards. See "Comptroller Stringer Launches Boardroom Accountability Project 3.0, a First-in-the-Nation Initiative to Bring Diversity to Board and CEO Recruitment," Office of the New York City Comptroller (press release), October 11, 2019.

4 See *United States Proxy Voting Guidelines*, Institutional Shareholder Services, November 18, 2019, p. 11.

5 See "Improving Corporate Governance through Diversity Act of 2019," H.R. 5084—116th Congress (2019-2020), which passed the US House of Representatives on November 19, 2019. Also see the letter sent by the US Chamber-led group of organizations to the US Senate Committee on Banking, Housing, and Urban Affairs on July 27, 2020.

6 See "A Push to Get More Women on Corporate Boards Gains Momentum," *NPR Morning Edition*, March 5, 2020.

7 *Every Other One: A Status Update on Women on Boards,* Policy Brief, The Conference Board, Committee for Economic Development (CED), November 14, 2016.

8 Assembly Bill No. 979, California Legislature—2019-2020 Regular Session, as passed in the State Senate on August 29, 2020. Under the new law, "Director from an underrepresented community" means an individual who self-identifies as Black, African-American, Hispanic, Latino, Asian, Pacific Islander, Native American, Native Hawaiian, Alaska Native, gay, lesbian, bisexual, or transgender.

9 The US Equal Employment Opportunity Commission (EEOC) is the public agency responsible for enforcing federal laws that make it illegal to discriminate against a job applicant or an employee because of the person's race, color, religion, sex (including pregnancy, gender identity, and sexual orientation), national origin, age, disability, or genetic information. Learn more at eeoc.gov.

10 *Systems Rule: How Board Governance Can Drive Sustainability Performance*, Ceres/KKS Advisors, 2018; Mark Emanuel, Todd Sirras, and Matteo Tonello, *Director Compensation Practices in the Russell 3000 and S&P 500: 2020 Edition*, The Conference Board/Semler Brossy, May 2020.

11 See, for example, *2019 Corporate Governance Principles and Proxy Voting Guidelines*, SBA Florida State Board of Administration, 2019, p. 14.

12 See *2019 UK Board Index*, Spencer Stuart, 2019, p. 4 (based on a review of the 150 largest companies in the FTSE index).

13 The main proxy advisory firms (ISS and Glass Lewis) explicitly voice their opposition to director term limits and set voting policies rejecting both management and shareholder resolutions on term limits. However, Glass Lewis adds that, where term limits are in place and they are violated, it may recommend shareholders vote "against" an incumbent director; and ISS urges shareholders to scrutinize boards where the average tenure of all directors exceeds 15 years. See *2020 Proxy Paper Guidelines—United States*, Glass Lewis, 2020, p. 24; *United States Proxy Voting Guidelines*, Institutional Shareholder Services, November 18, 2019, p. 17. Some institutional investors (e.g., BlackRock, Vanguard) are supportive of term limits only in situations where they are proposed by the board itself. They recognize that there may be situations where this tool is needed by the company to accelerate change. However, even these investors have a voting policy against term limits proposed by other shareholders. See *Corporate Governance and Proxy Voting Guidelines for U.S. Securities*, BlackRock Investment Stewardship, January 2020, p. 6; *Summary of the Proxy Voting Policy for U.S. Portfolio Companies*, Vanguard Funds, April 2020, p. 16. While stopping short of supporting shareholder resolutions on director term limits, other large institutional investors (Allianz, Amundi, CalPERS) vouch for additional scrutiny of boards with directors who have been in their position for 12 years or longer. See *Corporate Governance Guidelines*, AllianzGI Global, May 2018, p. 5; *Voting Policy 2020*, Amundi Asset Management, 2020, p. 13; *Governance and Sustainability Principles*, CalPERS, September 2019, p. 17.

14 On the benefits of tenure diversity, see, for a recent example, Na Li and Aida Sijamic Wahid, "Director Tenure Diversity and Board Monitoring Effectiveness," *Contemporary Accounting Research* 35, no. 3, Fall 2018, pp. 1363–1394.

15 Some of these policies do set specific restrictions for audit committee members (e.g., restrictions such as two or three additional audit committee services) but not for other members of the board.

16 Matteo Tonello, *Proxy Voting Analytics (2016-2019) and 2020 Season Preview*, The Conference Board/Russell Reynolds Associates/Rutgers Center for Corporate Law and Governance, December 2019, p. 11.

17 *Proxy Voting Guidelines for U.S. Portfolio Companies*, Vanguard Funds, April 1, 2019, p. 4. In the 2020 edition of its guidelines, Vanguard clarified that, despite these standards, it may still vote "for" overboarded directors if "company-specific facts and circumstances…indicate the director will indeed have sufficient capacity to fulfill his/her responsibilities" or "if the director has publicly committed to stepping down from the other directorship(s) necessary to fall within the thresholds listed above." *Summary of the Proxy Voting Policy for U.S. Portfolio Companies*, Vanguard Funds, April 1, 2020, p. 4.

18 *Corporate Governance and Proxy Voting Guidelines for U.S. Securities*, BlackRock Investment Stewardship, January 2020, p. 4.

19 See Rusty O'Kelley, Paul Rodel, Matteo Tonello, and Paul Washington, *Corporate Governance Challenges in the COVID-19 Crisis. Findings from a Survey of US Public Companies*, The Conference Board, June 2020. In particular, the survey revealed the exceptional time commitment required of board members at smaller companies.

20 When a board is classified, directors are organized into two or three classes; each class faces election every two or three years. Under most state laws, the default rule provides for all directors to be elected annually. However, to make it more difficult for hostile or activist shareholders to gain control of the board, organizational documents (charters, initial bylaws, or bylaws adopted by a majority of shareholders) can prescribe the longer, staggered terms of a classified structure: in this case, the activist must win more than one proxy contest at successive shareholder meetings to elect a majority of the board members and exercise control of the target. See Lucian Arye Bebchuk, John C. Coates, and Guhan Subramanian, "The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence, and Policy," *Stanford Law Review* 54, 2002, p. 887.

21 Matteo Tonello, *Proxy Voting Analytics (2016-2019) and 2020 Season Preview*, The Conference Board/Russell Reynolds Associates/Rutgers Center for Corporate Law and Governance, December 2019, p. 22.

22 Steven J. Choi, et al., "Does Majority Voting Improve Board Accountability?" *The University of Chicago Law Review* 83, 2016, p. 1157. The authors attribute their findings to the increased responsiveness to shareholder concerns that typically follows the change in the director election standard.

PUBLISHING TEAM

DESIGN	Peter Drubin, Maria Cristina Rueda
GRAPHICS	Ray Vella
EDITOR	Sara Churchville
PRODUCTION	Chris DiStasio