Ferguson Partners

Corporate Governance Monitor

Spring 2022

In the current edition of Corporate Governance monitor, Ferguson Partners shares recently published industry perspectives on current and critical Board-related issues.

Ferguson Partners REIT Diversity Study Finds Expanding Diversity

Ferguson Partners recently completed its annual analysis of REIT diversity across Boards and leadership through the lens of diverse representation with respect to gender, race and other underrepresented minority groups. Now in its fourth year, Ferguson Partners' REIT Diversity Across Boards and Executives analyzes Director and leadership demographics across U.S. public REITs.

Diversity, Equity, and Inclusion (DE&I) has continued to garner widespread attention among a variety of constituencies (most importantly, investors).

Topline findings include:

- 4th straight year that at least 50% of all new REIT Directors were female and REITs having outperformed the Russell 3000 in this regard
- 2.8% of REITs have zero female representation
- 12.7% of REIT Board members are minorities

- 39% year-over-year uptick of female leadership across named executive officers (NEOs) and leadership roles on Boards
- 42.5% of new REIT Board seats were minorities, nearly consistent with the 42% reported across the Russell 3000
- 48% year-over-year increase in the number of Committee Chairs that are led by minorities, though represent less than 10% in total
- 55% year-over-year increase in the number of Lead Directors/Chairpersons of the Board that are led by minorities, though represents less than 10% total
- 70% year-over-year increase in Black Board members going from 67 to 114
- 135% increase across 2018-2021 of REIT Boards that have at least 3 female Directors

Over a span of just four years, DE&I has quickly evolved from considerations of gender diversity across the Board room to all forms of diversity including gender, race, ethnicity, and sexual orientation – and not just at the Board level, but also across executive leadership and company employees as a whole.

Definitions of diversity, requirements of such, and disclosure items have sharply gained momentum and are now a focal point across institutional investors, proxy advisory firms, state regulators, as well as the Securities and Exchange Commission (SEC) and NASDAQ.

To learn about recent developments over the past year as well as announced 2022 requirements, download a PDF version.

Anti-Racism 'Imperative' Starts With C-Suite

Companies have pledged millions of dollars toward diversity, equity and inclusion initiatives and philanthropic efforts since the murder of George Floyd in May 2020 spurred companies to take action on systemic racism. But those efforts won't be successful unless corporate leaders do more to listen to employees and create a common, companywide language around DEI. They also need to be transparent on what their companies are measuring.

"When Black people, for example, see an organization making community investments, and yet inside [the company], the Board is not diverse, executives are not diverse, and employees are having a bad experience or face harm and deal with toxic leaders, it's a credibility buster," said Tara Jaye Frank, founder of leadership consultancy firm TJF Career Modeling.

"This is a topic area that needs to be a high priority," said James White, former CEO of Jamba Juice, current chair of the Honest Company and lead independent director at Affirm, Inc. "The nature of this issue has really been strengthened given the pandemic and the racial reckoning of 2020. You are going to see the discussions focused on the need for oversight and governance moving forward. Leaders have to educate themselves."

Board Oversight Needed

Companies should require high-level board oversight of anti-racist and DEI initiatives, said White, whose book, "Anti-Racist Leadership: How to Transform Corporate Culture in a Race-Conscious World," will hit the shelves in March. The best boards, he said, should review these issues "at a minimum" several times a year, and more focused boards review this quarterly. It's the board's role to ensure accurate and vetted public reporting of DEI initiatives.

This includes disclosing employee demographic data, for example, or risking losing reelection votes for directors on the committee in charge, such as the comp committee, said Ashley Marchand Orme, Director of Corporate Equity at Just Capital. For example, State Street Global Advisors has said it will vote against compensation committee chairs at companies that do not disclose EEO-1 data.

Companies can also consider pushing the envelope by disclosing inclusion, retention and promotion rates by demographics and role, Orme said. Indeed, 94% of the 100 largest U.S. employers disclose racial and ethnic diversity data, according to Just Capital, but only 32% disclose pay equity policies.

CEOs Should Bring DEI 'to Life'

In Frank's work with CEOs, she's found that when CEOs are declarative about DEI goals, setting targets and goals along with accountability mechanisms, the rest of the C-suite will follow suit. But, for companies with CEOs that want to "do the right thing" without anything formal in place, "those companies make zero progress. They lose ground because there is no agreed-upon standard on what equity and inclusion looks like."

White also encourages companies to tie specific DEI metrics directly to executive compensation. Companies such as American Express, FirstEnergy, Invesco and Verizon do this, as reported by Agenda.

Employee-Focused Strategies

Frank said companies need to fully understand what employees are experiencing inside the company's walls, which is different than measuring engagement or sentiment.

> *"If you understand what employees are actually experiencing, you can predict the degree to which they will stay and recommend others to join the company, as well as the degree to which they feel they belong," Frank said.*

Frank said companies need to focus on representation as opposed to setting targets for a certain number of women or minorities. For example, she advises companies to take a close look at the consumer base and make sure it is represented throughout the company.

Workers Value a Good Work Culture Over Pay, Says Report

There is good news and bad news for companies looking to retain their workers amid unprecedented turnover of U.S. personnel who have left the workforce or switched jobs looking for better opportunities in the last year.

Over 1,000 full-time U.S. employees were surveyed recently about their career prospects and sentiments toward their workplace for a January report by the research company PlanBeyond. Almost half, 42%, of the respondents between the ages of 18 and 64 said they plan to quit their jobs in the next six months.

As Boards face increasing pressure to wrap their arms around human capital management issues, the silver lining for companies is that, though they could be time-consuming to remedy, the matters employees are mostly dissatisfied with may not be too costly to fix.

Most of the respondents were concerned about poor workplace culture, while concerns about fair pay were lower down on the list of priorities, according to Laura Troyani, the author of the report and the founder of the Seattle-based enterprise.

The top reason for workers' dissatisfaction with their current workplace, as cited by over one-fifth of the surveyed professionals, was feeling "underappreciated" by their companies.

The second reason for worker malcontent was bad supervisors, chosen by 18% of the respondents. In third place, 16% of workers said a lack of freedom of expression or their inability to be their authentic selves at work drove their desire to quit, while 11% cited bad colleagues as a reason for their impending departure. Low pay was further down in the order of priorities, cited by 6% of workers as the greatest source of their dissatisfaction.

The report categorized salary and workplace flexibility as hard issues, while human relations were soft factors that may be harder to measure and fix, according to Troyani.

"What was especially surprising was that the hard factors were almost insignificant in most cases, be it for male, female workers, young and old. They weren't terribly impactful," said Troyani. "If you're a manager looking at your organization's attrition

patterns and wondering what you can do to stave that off, our data is showing you've got to look at the soft factors. But getting a manager to be a good manager is actually a lot harder than saying, 'I am going to increase your hourly wages.'"

The wave of employee turnover, which some market watchers have called the Great Resignation, may not abate soon, according to experts.

A record 4.5 million U.S. workers left their jobs in November, according to data from the U.S. Bureau of Labor Statistics. Workers between the ages of 30 and 45 were the largest cohort who resigned.

Pay was a major reason for employees quitting if they made around or below $30,000 a year, but workers making more than that amount valued quality of life and work issues more, according to PlanBeyond's report.

Protests from Within: Engaging with Employee Activists

In recent years, we have seen a growing trend of stakeholder issues becoming prominent in discussions of corporate governance. This phenomenon is broadly known as ESG (environmental, social, and governance) and is characterized by pressure on companies to increase the attention they pay to and the investment they make in initiatives to advance the interests of all stakeholders—not just shareholders—including employees, suppliers, customers, and society.

Per some governance research from Stanford University, one source of this pressure comes from an unexpected constituent: the company's own employee base. To a greater extent than in the past, workers are pressuring employers to take policy stances and advocate on behalf of social, environmental, or political issues not necessarily directly related to the company's core business. The issues involved are extremely broad and include environmental sustainability; reducing waste, pollution, or carbon emissions; workplace equality; diversity and inclusion; human rights violations; immigration policy; government defense contracting; gun control; free speech; and protesting statements of policymakers or politicians. Employee activism is related in spirit to unionization efforts—the crucial difference being that unionization efforts focus on improved working conditions for employees (through wage increases, benefits, safety, etc.) while activism encourages broader social and political activity which may or may not benefit an individual employee.

There are a variety of approaches that companies might take to mitigate the risks of employee activism. Although their ultimate approaches differ significantly, they share common elements.

These include:

1) Mission and Purpose.

The company develops a clear mission and value statement. This can be narrowly or broadly construed—meaning it can be strictly shareholder-centric or can be broadly inclusive of stakeholders—so long as it is clearly defined. A clear mission statement specifies the scope of activities that the company will and will not engage in and provides a framework for the board and management to use to evaluate stakeholder-related claims within the context of the company's value-creation model. It also allows the company to express that it has a conscience for achieving social good within the sphere of its business activity.

2) Communication.

Management clearly and consistently communicates its mission and values to internal and external constituents. By specifying the demarcation line of the company's activities, the company sets boundaries for employee expectations on the issues it will engage in, while still exhibiting the social empathy that many employees are seeking from the companies they work for. Communicating this information in advance can forestall more extreme forms of employee activism that are distracting to the company.

3) Oversight and Implementation.

The company remains consistent in its approach to investing in ESG-related causes at the heart of many employee activism events. Consistency prevents "mission creep," and keeps the conversation focused on the activities that management is willing to engage in. A key challenge will be to maintain the flexibility required to respond to changing circumstances without losing control of the overall ESG agenda. Obviously, companies need to make sure that employees know about their commitment to ESG, and perhaps even include employee groups in this discussion.

Surge in Talent Oversight Work for Boards

An overwhelming majority of Directors are spending more time on talent management in Board work, with such issues as the retention of key executive and nonexecutive talent and the oversight of complex multigenerational workforces emerging as high-priority issues.

The annual Achievers Workforce Institute survey found that 44% of U.S. respondents say they plan to look for a new job in 2022, while 22% are undecided, compared to global results of 41% who plan to job hunt and 25% who are unsure. The annual engagement and retention survey tracked 5,500 respondents in different countries between December 2021 and January 2022.

In certain industries and among employees with specific expertise, the turnover issue is severe and competition for talent is acute. A 2021 LinkedIn study revealed a 13.2% turnover rate in the tech industry, which companies of all stripes look to for internal tech talent. Among certain software engineers, the turnover rate reached 21.7%, the study found.

Meanwhile, younger generations are accustomed to using technology in different ways than older generations and having perspective in the boardroom about how that will impact companies' strategies and internal workforce trends can be helpful.

Indeed, that trend in recent years has prompted some companies to combine employee experience, engagement and technology into a single role at the executive level, as Agenda has reported. At Salesforce, the company appointed a former chief technology officer to become vice president of enterprise IT and employee experience, while Raytheon named an executive vice president of digital workplace and employee experience. Similarly, JPMorgan broadened its chief information officer's role to an employee experience role focused on updating the company's internal technology for employees.

Broadly, challenges in retention and hybrid workforce issues have been elevated to the Board level because they have a significant impact on compensation policies. Given the pandemic and remote work, employees and executives have reassessed their priorities about work and life at a time when it's a lot easier, practically speaking, for employees to accept incoming calls about opportunities and to negotiate interviewing and accepting new positions, she said. The barriers to changing jobs have decreased dramatically.

The increasing focus on talent oversight also partially stems from greater oversight of ESG. Those trends have led to increased receptivity among board search committees to consider candidates with experience as general counsel or head of human resources, particularly if those candidates also bring greater diversity to the board in terms of gender, race and ethnicity.

Portions of the included articles, originally published in Agenda, Stanford Closer Look Series, have been edited for length and clarity. Authors include Lindsay Frost, Amanda Gerut, David F. Larcker, Stephen A. Miles, Neanda Salvaterra, Brian Tayan