Compensation Committee Leadership Network

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CCLN

VIEWPOINTS

Discussions on gender equity and CEO assessment

Compensation committees are not impervious to the pressure on corporate boards to address new topics or novel approaches to longstanding issues. The increasing urgency to achieve gender equity—including but not limited to pay equity—has changed the agendas of several Compensation Committee Leadership Network (CCLN) members' compensation committees. In addition, members seek to evaluate the effectiveness of their CEO assessments.

On October 29-30, CCLN members met in Washington D.C. and were joined by Lori Nishiura Mackenzie, Executive Director of Stanford University's Clayman Institute for Gender Research and co-founder of the Stanford VMware Women's Leadership Lab, and Stephen Miles, founder and CEO of the Miles Group, to discuss opportunities to address these issues and other topics of interest to committee members. This *ViewPoints* synthesizes those conversations.[1]

Gender equity

While differences in pay narrowed steadily for many years, progress has stalled in the last decade, and the upper echelons of management remain a male-dominated realm. In 1980, women's full-time weekly earnings were 64% of men's, according to the U.S. Bureau of Labor Statistics. By 2005, they were 81%, but by 2017, they were still just short of 82%.[2]

This overall gap is due partly to different job types and to seniority but even controlling for these differences, there is still a substantial gap: a study by researchers at Glassdoor estimated that 33% of the wage gap in the US is unexplained.[3] Ms. Mackenzie noted, *"The gender pay gap is lowest for people graduating college. Then as women continue into their childbearing years, the gap widens and continues to grow regardless of whether or not they have children or leave the workforce."* Advocates argue that the pay gap is just a piece of a broader issue. The factors that cause women to be paid less for the same work may also cause them to be hired and promoted less often.

The representation of women in senior management remains very low. Research by Compensation Advisory Partners found that fewer than 50% of companies in a sample of 150 large U.S. companies had any named executive officers who were women; only 7% had a female CEO.[4] Ms. Mackenzie said, *"For many years, there has been broad interest in the business community in how to do a better job hiring women and then how to advance women into leadership. But we have seen zero progress in the past decade on this front. In fact, this year, the rate of women CEOs has declined by 25% and there is no black female CEO in the Fortune 500."*

Understanding the problem

There are many factors that contribute to gender pay discrepancies and a lack of women in leadership roles. CCLN members discussed a number of these issues with Ms. Mackenzie:

- **Unconscious bias**. One underestimated factor that leads to gender inequity in the workforce relates to societal stereotypes about certain groups of people. *"We all carry some level of unconscious bias based on the way we grow up and our experiences,"* one member said. Ms. Mackenzie expanded on the concept: *"the paradox of meritocracy is that when people believe the system to be fair, they as managers actually become more biased*."
- **Definition of leadership.** Ms. Mackenzie said that when companies consider candidates for promotion, they look for a set of characteristics that tend to be linked to males: *"Leadership is linked to adjectives like visionary, driver, genius. But when we think genius, we think Einstein not Marie Currie. We also think of men first when thinking of visionary, driver, or leader itself."* She added that the characteristics that are more commonly linked to women are frequently overlooked or downplayed when hiring senior leaders: *"Are people being promoted in your organizations based on their collaborative expertise? Usually no. But those skills are ones that drive positive outcomes."*
- **Failure to negotiate.** Ms. Mackenzie noted that even when graduating from the same university with the same grades and same degree, men receive a slightly higher starting salary than their female counterparts. Why? *"Men were negotiating, and women were not. For men and women MBA's there is a 7% pay gap—it's small but it leads to a much larger gap over time,"* said Ms. Mackenzie. One member added, *"Some of the problems we see are the manifestation of societal problems. Men are more willing to negotiate pay—and are therefore paid more initially and over time—because they are brought up to be more aggressive."*
- **Gendered pathing of careers.** *"Gendered pathing occurs when two equally qualified individuals enter the workforce and their careers lead to different paths with different pay. For example, in the tech sector, there is the engineer path that leads to Chief Technology Officer or the product path that leads to Vice President of Engineering. Both require a computer science degree but the pay in the two tracks [is] different. Ultimately, only one path leads to leadership and that path tends to have fewer women,"* said Ms. Mackenzie.
- **Timelines for promotion.** Ms. Mackenzie discussed the "70/20/10" hypothesis for career development which states that 70% of skills for promotion come from experience on the job, 20% from critical relationships, and 10% from education on the job. She further pointed out, *"A lot of mentorship is given to women but little attention is paid to the 70% of this equation. Women are not receiving the critical assignments needed to advance to the next level, usually due to less visibility to senior management."* One member added, *"When it*

> *comes to promotions, women tend to stay longer in their roles. If the job says it requires 10 skills, women will not apply unless they have at least 9. Men see the same requirements and apply with only 2 of the skills required. Women hold themselves back by thinking they need to prove themselves before they even start the role."*

Not all companies have the same problems when it comes to gender inequity. CCLN members said it is important for companies to understand gender equity within their own organizations. For pay differences, this involves looking at salaries by gender and analyzing the potential reasons for any differences, which could include not only differences between jobs but also differences between credentials, experience, and other qualifications. Several members commented on their companies' extensive analysis. One said, *"My company has published a gender equity report for many years now. We have tons of data by geography, by gender pay, promotion, bonus, title, etc. We are working on diversity stats now too."*

Some companies undertake sophisticated modeling to identify residual effects that might be explained by gender discrimination. One member said, *"When looking at our data, if there is a management issue—it jumps right out at you. Maybe not by pay but it could be by advancement. Why are women not moving up under this leadership? You can easily see where you need to dig deeper."* Another emphasized the importance of going beyond aggregated data to look at the data for specific business units: *"It's important to drill down in the data to look into specific departments, and even specific roles, to see if you can pinpoint an issue."*

Implementing solutions

If there is a gender gap that cannot be readily explained, experts recommend that companies adjust policies and even salaries as well as establish new programs to address prominent issues. Salesforce, for example, spent $6 million on pay adjustments after an analysis revealed gaps based on gender and ethnicity.[5] One member asked, *"What is your view on solving an inequity problem by making an adjustment in pay for women?"* Ms. Mackenzie responded that, *"It works if you are checking the numbers every year and solving for inequity on an annual basis."* She noted, however, that in most cases the issues go beyond pay equity and therefore require more systemic solutions than just closing the pay gap.

The following approaches to creating gender equity are often highlighted by experts and were mentioned by CCLN members:

- **Formalizing processes.** Members acknowledged that informal, subjective decisions in the processes used to hire, promote, and compensate people are a direct cause of gender inequity. Bias is especially prevalent when the criteria for decision making are ambiguous. It is therefore important for companies to follow more detailed, defined processes for hiring and promotions. Ms. Mackenzie offered some tips: *"Be very clear and fair about the criteria you are using for every [personnel] decision— hiring, promotions, performance management. We know from research that when you first agree to criteria, then make a*

decision, you are less likely to make biased decisions. Bias also thrives in ambiguity: forms with blank spaces and open boxes are an opportunity to introduce bias."

- **Stated diversity goals.** Setting gender diversity goals can help as well. One member said, *"It's not about setting quotas but targets. If we have a target and a method for tracking performance, it is very powerful because it brings transparency and accountability."* Ms. Mackenzie added, *"If you are to use quotas, you may have more success to use them on interview lists as oppose to having percentage diversity quotas at each level of the organization. Requiring a pool of candidates with 30% diversity is an example of quotas bringing about a positive outcome. This also helps to prevent the perception of someone being a 'diversity hire.'"*
- **Block-bias training.** Training can make managers aware of their unconscious biases and help counter them.[6] However, Ms. Mackenzie cautioned, *"Educating people on unconscious bias, in isolation, can actually do more harm than good. You normalize the behavior, so people stop scrutinizing their behavior and open themselves up to even more bias. You want to train employees through the lens of awareness and accountability: 'if unconscious bias does exist, we will do everything we can to debug how it works in our organization.'"* A member agreed, noting, *"We need screens to catch ourselves and our organizations, so that we don't always make the comfortable decision*."
- **Support programs.** Mentorship and training programs that help women develop their leadership skills and professional networks can accelerate their rise through the ranks. Ms. Mackenzie mentioned one company policy that requires leaders to have a diverse suite of mentees but does not dictate the mentor's choice of mentees. Many members agreed that this approach worked better than formally assigned mentorship programs. Sponsorship programs, in which someone actively advocates for a person, can help others recognize a woman's achievements and suitability for key assignments.[7]
- **Flexibility.** Flexible work schedules and generous parental leave programs can help attract and retain a diverse group of employees. Making it easier for women and men to meet family obligations makes it easier for them to accept higher-level jobs.[8] However, one member raised concerns, *"Because more women are in these remote roles and have flexible arrangements, does the lack of facetime hold them back? We are moving very quickly on this in some cases and I don't know if it is hurting the mission we are actually trying to accomplish."* Ms. Mackenzie cautioned, *"If you don't have the right controls in place, women can end up being penalized for remote work. Flexible work policies need to be framed as a new workplace structure, not as an aid to women. Have policies and clarity about career trajectories in place so that people taking the flexible work will not be harmed. People need flexibility and stability together."*

Establishing and fine-tuning these policies and programs may require commitment from the highest corporate ranks. It may also require outside expertise, especially when new initiatives

are first rolled out. One member suggested carefully using targets to implement new programs: *"Targets can be powerful—they encourage transparency and accountability and help us track and measure progress. But they also require a certain degree of flexibility."*

Ms. Mackenzie provided some additional context on how to avoid bad decisions: *"Sometimes people ask me if bias is salient in all conditions: the answer is "no." There are three conditions when additional bias is introduced: (1) when operating in a crisis; (2) when there is ambiguity in decision making; and (3) when definitions of success are very narrow. Reduce these conditions to allow for men and women to be assessed equally."*

Leading from the top

CEOs and boards face pressure as public attention and external forces have elevated gender equity issues beyond the human resources function. In some cases, CEOs are facing public pressure from investors—as well as private pressure from employees—to advocate for pay equity. Members added that gender equity is among several social responsibility issues that are taking up more board time.

Members discussed how boards can play a broader role in ensuring gender equity across their organizations. Several suggested taking a closer look at the data provided by management and following up on potential areas of interest. One explained a periodic, retrospective review of management's hiring process: *"We look at the talent pool to be sure it is diverse. We won't tell management who to choose for a position but we will look at the number of opportunities they have had to hire women to see if there is a trend of a problem over time."*

Like diversity within senior management, gender balance on the board has become a prominent issue in recent years. In several European countries, a minimum level of representation is mandated, and in the United States, California recently became the first state to mandate that all publicly traded companies with headquarters in the state have a certain number of women on the board: initially one, then more by 2021 depending on company size.[9] One member suggested that progress trickles down from the top: *"In my career, I was used to being the only woman on the board. It was fine, but you did feel like you carried a bit of a diversity flag. Once you get to four women on the board it's fascinating because the whole culture changes. If you look at the board as an extension of the organization you see that you do need a critical mass to propel diversity of thought. And I think when it starts at the top, it pushes down into the organization."*

CEO assessment

While the CEO is typically assessed against financial targets to determine compensation, most boards also engage in a broader evaluation intended to help the CEO improve performance in a range of other areas. The compensation committee often has incremental responsibility for this process.[10]

Not that long ago, feedback from the board was often shared in a brief hallway conversation with a director, often the compensation chair, and the only metrics discussed were company financial targets. While those approaches still exist, the process at CCLN member companies is generally more robust. CCLN members highlighted several elements that are frequently part of the process:

- **The CEO drafts objectives.** The board asks the CEO to specify achievement objectives. The board reviews and, if necessary, rewords these objectives, which then serve as benchmarks for the following year or more. Identifying the most important objectives is critical. *"Our CEO typically lists 12 objectives and we have a healthy discussion at the board level and bring that number down to five,"* one member shared.

- **The CEO provides a self-assessment.** A particularly important source of feedback is the CEO's self-evaluation. Careful reflection and candor are key, members said, particularly on developmental opportunities. *"I think it's a positive when a CEO focuses on the negative,"* one member said. Mr. Miles shared an effective means of getting the CEO's self-assessment: *"Having the CEO deliver remarks about his or her performance during a board dinner can be very powerful. There's something about the formality of the board meeting and the intimacy of the dinner that just works. The CEO can then leave before dessert when the board can discuss the assessment in executive session."*

- **The board gathers feedback from its directors.** There are several ways to gather board input on the CEO, ranging from do-it-yourself interviews, electronic tools, and outside vendors, commonly attorneys. Members said the challenge is balancing the depth and quality of the feedback with the burden of the process.

- **The board gathers feedback from the CEO's direct reports.** Members had an active debate about the costs and benefits of getting feedback from top executives. One member finds value "*in the differences between the board's assessment of the CEO and the assessment provided by h*is or her direct reports." Mr. Miles noted that, *"Management referencing needs are relatively rare and, when it is done, it is important to separate it from the end of year compensation discussion and keep it focused on development. If a board is going to do one, it should be careful to avoid falling victim to … data that has been 'gamed,' and it should be careful to make sure it responds appropriately to the feedback. There is the risk that the board creates distrust with the CEO or the managers if it either over- or underreacts to the feedback."*

- **Deliver feedback to the CEO.** The last stage of the process is to discuss the results with the CEO. In addition to sharing feedback from the more comprehensive annual review, most CCLN members have a process for providing regular feedback after each board meeting. That is especially true if there is an issue of concern to the board. "*It's important not to wait until year end if something isn't going well,"* one member said. In both cases, many suggested that two directors be involved. One member said, *"That helps make it*

clear that this is feedback from the board, not a director." Mr. Miles noted, *"A 2:1 approach for delivering feedback to the CEO tends to work well because the CEO is less likely to think she is being picked on by a single director with a personal agenda. The feedback needs to represent the views of the board."* He added that these sessions are most productive when the board demonstrates a detailed knowledge of the CEOs strengths and areas for improvement: *"The truth is, no one really wants negative feedback, even if they ask for it, and the easiest thing to do is make someone cry. The goal of all feedback is to encourage someone to try something new or do something different. Deliver feedback holistically, the good and the bad, and keep it short and specific. Always keep in mind where you are on the journey with your CEO, whether it is the first or last inning. The key is to start CEO feedback with your newly appointed CEO and make it something you do as a board."*

Depending on the company, industry, and individuals involved, the substance of the feedback will differ, but members identified three important skills they look for when evaluating the CEO:

- **Strategic mindset**. *"The assessment process is closely linked to the strategy and strategic objectives,"* one member said. The ability to manage today's business while preparing the company to succeed in the future is essential. As Mr. Miles put it, *"The strategy of any successful CEO is to win the business of today and to build the business of tomorrow."* Mr. Miles suggested, *"Ask yourself, are you getting what you need from the CEO and if not, is there someone surrounding him in leadership that can fill that void? We talk about succession planning in terms of a single person event, that we need to pick our next CEO. Succession is actually a multi-person event and complimentary skills on the team can allow you to take on more or less risk on your candidate."* One key manifestation of this strategic mindset is an appropriate focus on succession planning. *"We ask the CEO to include a bit about succession planning and her term vision in her self-evaluation,"* one member said.
- **Empathy at a distance**. Having a CEO who can understand how issues will be perceived by important stakeholders—customers, employees, business partners, and the public—can avoid reputational damage, and this is more important than ever given how quickly news spreads. It can also help create goodwill. One member spoke of a CEO statement in an employee forum that was widely shared because the message resonated: *"We did not know it was being taped and would end up on social media, but it did. Luckily it was a great response. Positive things can go viral, too."*
- **Capacity for learning.** The ability and desire to learn can separate the good from the great and can help a CEO grow into the role. Members said that an aptitude for continuous improvement is a critical element to a CEO's long-term success. Mr. Miles said, *"If a CEO can take feedback well and is willing to learn from it and wants to develop, focus on what is material. Pick one or two specific areas for improvement and*

be sure to include plenty of discussion on strengths when the feedback is presented." Mr. Miles underscored the importance of finding a CEO who can absorb and synthesize advice from a range of content experts and good advisors, *"ultimately, for the CEO it comes down to what he or she learns after they 'know it all' and that is what counts."*

Clawback policy revisions

A wave of recent scandals has led many compensation committees to reassess how and when they can claw back compensation for management misconduct. Committees are considering whether to move away from more traditional "double trigger" clawback policies—where clawbacks are only permissible in the event of both misconduct and a financial restatement—and adopt policies that authorize discretionary clawbacks, even absent restatement. One member said, *"We revised our policy to give our committee broad discretion. We got lots of positive feedback. It says something if management will fight on this."*

Meridian Compensation Partners' Annette Leckie said, *"We've seen public examples of scandals where executives have gotten no bonus and lost their jobs, but they did not forfeit unvested equity or have any prior compensation clawed back. It's hard to know whether that outcome was the result of a narrowly defined clawback policy, or what the board felt was the right answer. Therefore it's important that boards make sure they have the right clawback and forfeiture tools in place before a situation occurs."* Meridian expects a number of boards to broaden their clawback authority this proxy season. John Anderson said, *"If you benchmark against peers today using 2018 proxy disclosure, you might not see much change, but if you look next year, I think you may see a big move to broader clawback policies."*

For example, Glass Lewis recently clarified its views on clawbacks noting that it would examine policy terms and whether they go beyond minimum legal requirements. Previously, it simply noted whether or not a company had a clawback policy.[11]

About this document

The Compensation Committee Leadership Network (CCLN) brings together compensation committee leaders from North America's most prominent companies for private discussions about improving the performance of their corporations and earning the trust of their shareholders. *ViewPoints* is produced by Tapestry Networks to stimulate timely, substantive board discussions.

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Appendix

The following directors participated in the meeting:

- John Anderson, Meridian Compensation Partners
- Beth Cobert, CBRE
- Erroll Davis, Union Pacific
- Marianne Harris, Sun Life Financial
- Jim Kennedy, United Continental
- Annette Leckie, Meridian Compensation Partners
- Karen Maidment, TD Bank Group
- George Munoz, Altria
- Joyce Roché, AT&T
- Virginia Ruesterholz, Frontier Communications and The Hartford

The following directors took part in discussions before or after the meetings:

- Mel Lagomasino, The Coca-Cola Company

Endnotes

[1] *ViewPoints* reflects the network's use of a modified version of the Chatham House Rule whereby comments are not attributed to individuals, corporations, or institutions. Network participants' comments appear in italics.

[2] Ariane Hegewisch and Emma Williams-Baron, *The Gender Wage Gap: 2017 Earnings Differences by Race and Ethnicity*, (Washington, D.C.: Institute for Women's Policy Research, March 2018), Fact Sheet, Table 2.

[3] Dr. Andrew Chamberlain, *Demystifying the Gender Pay Gap: Evidence from Glassdoor Salary Data* (Glassdoor, March 2016), 3.

[4] Kelly Malafis and Michael Bonner, "Gender Pay Equity – What do Directors and Executives Need to Know?" *CAPintel*, May 7, 2018, 1.

[5] Amanda Gerut, "A Pay-Gap Fix Requires More Than Money," *Agenda*, April 2, 2018.

[6] International Labor Organization, *Breaking barriers: Unconscious gender bias in the workplace* (Geneva, Switzerland: ACT/EMP, August 2017).

[7] "Catalyst Study Shows Sponsorship is Key to Women's Success," Catalyst, accessed August 8, 2018.

[8] Jaclyn Jaeger, "Compliance's role in thwarting gender inequality rhetoric," *Compliance Week*, April 11, 2017.

[9] Vanessa Fuhrmans, "California Becomes First State to Mandate Female Board Directors," *Wall Street Journal*, September 30, 2018.

[10] Amanda Gerut, "Comp Committees Take Over CEO Reviews," *Agenda*, May 18, 2015.

[11] Eric Chen, Jim Kroll, and Alex Pattillo, "New Glass Lewis policy updates for North America highlight disclosure, diversity…" Willis Towers Watson, October 31, 2018.