CORPORATE BOARD MEMBER | Segal

Expanding Oversight of

HUMAN CAPITAL RISKS

Setting Your Board Up for Success

Human capital risks have been a rising concern for virtually every company since long before the pandemic hit. A dearth of workers with technical skills, the strengthening drive for diverse workforces and new reporting standards are among the challenges fueling the need to place talent front and center on boardroom agendas in recent years.

Covid lockdowns added new areas of concern to the mix. As Fred Hencke, senior vice president of Segal, told directors gathered for a discussion on effective oversight of talent: "2020 really accelerated the need to pay close attention to more aspects of human capital, including remote and hybrid work situations, the war for talent, social justice and changes to benefits and human resource compliance requirements."

Charged with helping management ensure that people remain one of their organization's biggest assets, directors find their oversight role growing in tandem with this ever-more-complex talent management landscape. Increasingly, challenges emerge from within and without, ranging from the growing use of social media by employees contributing to anxiety and isolation to how external incidents of social injustice impact morale and harmony in the workplace.

The Social Stance Dilemma

Whether and how to address public issues has long been a thorny dilemma for boards, with taking a stance on matters of controversy viewed as likely to alienate stakeholders as to mollify them or, better yet, unite them around a common purpose. It claimed an even larger spotlight over the past year, after incidents of racial inequity sparked public protests. Several directors participating in the roundtable recounted grappling with the need to weigh in on social injustice as employees and other stakeholders clamored for a response.

"When we thought about [the issue of social justice], it was a place where we felt we needed to say something, but we absolutely wanted to focus on what unites us, on everyone having a voice and feeling included and listening and seeking to understand," said Cindy Baier, president and CEO of Brookdale Senior Living, who reported that facilitating internal discussions was helpful. "We had a lot of listening sessions where people could share their perspectives, and that seemed to resonate within our organizations."

At Reinsurance Group of America, incidents of social unrest prompted the company to create new resource groups. "We reinvigorated and, in some cases, created new employee resource councils, and we're listening very hard to what those councils have to say," said Hazel McNeilage, a director at Reinsurance Group of America.

Valeria Roach, board member at CBI Global, views responding to incidents of racial inequity as an extension of both the board and management's overall commitment to diversity and inclusion initiatives. "Diversity, Equity and Inclusion (DEI) is a topic the board definitely owns, and where we want to ensure that there's clear understanding of what that means in terms of board and leadership responsibility," she says. "Our passion and our mission support vulnerable communities around the world. We applied that concept to our employees, making sure that everyone had an opportunity to share their emotions and input on how we can continue to change within the organization. We wanted to make sure that we address that from an ethical perspective in our code of business ethics, our stand and our tolerance level for behavior in the organization."

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—Fred Hencke, Senior Vice President, Segal

For many companies, the need for alignment around the organization's stance on issues dovetails with policies on social media. For Brookdale Senior Living, which has 45,000 associates working in 700 eldercare communities, employee posts about Covid on social media surfaced as a board-level concern early on. "We are constantly trying to make sure that what is portrayed on social media is consistent with our values," says Baier. "Whenever someone takes a stance that's inconsistent with that, then actions are taken by the company. Facebook actually recognized us as a leader in social media for our response to the pandemic."

Institutionalizing Pandemic Lessons

The pandemic—the epitome of an unanticipated external threat—played a part in helping some companies recognize the importance of coming together as a community to tackle difficult social issues. Even for multinational companies with employees spread out around the world, Covid represented a unifying challenge that resonated at all levels and in all locations.

"The pandemic brought home for us something that should have been obvious a long time ago, which is that we truly are all in this together," said Neil Novich, a director at W.W. Grainger, Hillenbrand and Beacon Roofing Supply, who describes the pandemic as a "common denominator" that fostered alignment. "It's not that we weren't discussing a variety of social issues before that, but not everyone can relate in a fulsome way to a every social issue—whereas everyone could relate to Covid simultaneously. As bad as this past year has been, I think it brought a new understanding of how interrelated we all are and that we have to think about that more in terms of a variety of social issues."

Renewed focus on employee physical and mental wellbeing, the importance of frequent and effective communication, a different approach toward flexibility and a new appreciation for what organizations are capable of are some of the learnings companies took away from operating through the pandemic. Hanging onto those as we move toward some semblance of normalcy may be the tricky part, notes Novich, who points to his experiences on audit committees as an example.

"Two years ago, if you had said, 'You have to do a complete internal and external audit without leaving your office,' we would have said, 'That's crazy talk,'" he said. "Yet, within weeks we had it all figured out. So, we learned a lot of things. Let's not forget those. Let's use them to improve the way we run our businesses in the future, including how we think about our associates, how we think about social issues. It would be horrible if we got through this and back to normal and just went back to our normal lives. We need to think about what we're learning today that we can apply over the next few years."

The Agility Advantage

There's a strong business case to be made for finding and institutionalizing the work that companies put into adapting quickly during the pandemic, added Hencke. "Strong leadership, transparency and a workforce of employees who are physically and emotionally well leads to a more agile organization—and organizations that are more agile outperform their peers in the market," he noted.

In fact, research from McKinsey & Co. suggests that agile organizations responsive to major threats and opportunities outperform those that are less agile by 93 percent on customer satisfaction, 76 percent on employee engagement and 93 percent on operational performance.

Agility, however, can be elusive. "The agility piece is how do we prepare for the next set of opportunities and challenges facing us in the future?" said Hencke. "Digitalization, for example, mapping your customer journey and translating it into how you provide a service or product to your customer, is not just technology, it's a behavioral change inside your organization."

Boards can play a pivotal part in helping companies step back from day-to-day operational challenges to visualize the

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big-picture, future-focused agility imperative. "Our board has been very helpful in making sure that we think strategically about the long term," said Baier. "When our business was at the center of the pandemic storm, they were the ones pushing us to make sure we were thinking about how to really capitalize on our leadership position as a result of the pandemic."

Embracing Flexibility

Flexible work arrangements is another area boards should push companies to continue exploring, noted Howard Fluhr, chairman emeritus of Segal. "Management needs to be open-minded about what their current employees want—what they will want after what they have been through during this surreal 13 months. What I'm seeing on the boards on which I sit is that smart companies are saying, 'We're going to experiment. We're going to get a lot of input, hold a lot of town halls and do a lot of surveys. There's a lot we've learned about human behavior and interactions that has staying power."

While some employees may be anxious to return to offices, others will balk—and taking a hard stance may backfire in today's talent market. In a survey by McKinsey & Co., 70 percent of employees said the ability to telecommute is an important factor for their next job. Furthermore, a whopping 54 percent report that they will change jobs for more flexible work options, said Hencke, who noted that younger generation employees tend to prioritize work-life balance when weighing employment options. "They saw their parents and grandparents work 60, 70 and 80 hours a week and not really enjoy their lives as much as they probably should have and they don't want to fall into that. That's really important because this is the generation we're recruiting."

"We're also seeing people willing to leave jobs tied to metro areas for telecommuting jobs that allow them to live where they can do things like hike, fish and spend more time with family," he said, adding that on the flip side, embracing telecommuting enables companies to widen their recruiting net. "Somebody living in Alaska or Hawaii may be a candidate, whereas last year he or she might not have been."

Still, making flexibility work on a more long-term basis will mean finding ways to replicate informal mentorship, collaboration and other interpersonal interactions that happen naturally in shared-office situations. Savvy companies will look for ways to redirect resources formerly devoted to physical space for employees toward fostering other ways of enabling interaction and collaboration—and still realize savings, said Novich. "Some companies are spending $25,000 a year per person on office space in New York," he noted. "That money could probably be used more cost effectively—it's a matter of taking charge of it as opposed to having it happen almost automatically because people are all in the same building."

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Source: McKinsey & Co.

Bring on the Metrics

The concept of looking for ways to value human capital and quantifying return on investments in areas like recruiting, managing and developing talent has been gaining momentum. In 2020, the SEC recommended discussion and disclosure on three primary areas including: human capital talent attraction, human capital development and talent retention, with workforce productivity and employee engagement as secondary areas of focus for discussion and disclosure. What's more, the International Organization for Standardization (ISO) recently introduced the ISO 30414 Human Resource Management Guidelines for Human Capital Reporting for Internal and External Stakeholders, the world's first global standard focused specifically on how to measure and report human capital both internally and externally (disclosure) for both small and large organizations.

"They're developing a whole series of metrics around human capital," explained Hencke, who sees human capital standards as a logical extension of other metrics frequently used to evaluate performance. "On average, human capital is 54 percent of the cost of an organization, so why would we not manage it, measure it and make it visible like we do other assets, such as financial and manufacturing assets? It's great to talk about attraction, development and retention, but we're going to need to start measuring things like how long it takes to fill new positions and how often people move around for promotions and new assignments at some point."

It's a concept that resonated with Novich, who reported that his company has been looking for ways to measure the toll the pandemic has taken on employee health and well-being. Applying greater rigor to recruiting and development processes makes business sense, he added, noting, "If any company is establishing a new supply chain, we would look to understand the supplier, their quality, where they get raw materials, their security policies. We would do a lot of work all the way down the supply chain, yet the majority of companies treat recruiting with far less deliberation."

The need to take a more intentional, strategic approach to all the facets of human capital management will only intensify in the digital age. "At the end of the day, it's employees who determine how well companies do at aligning strategies, structures, processes, leadership roles and responsibilities," said Hencke. "They're at the center of all of that, and that's only going to increase."