

REPORT OF THE NACD BLUE RIBBON COMMISSION

2020 UPDATE OF THE
**DIVERSE
BOARD**
MOVING FROM
INTEREST TO
ACTION



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2020 Update of The Diverse Board 2020: Moving From Interest to Action

Curtis Crawford, the Honorable Cari M. Dominguez, William McCracken, and Kathi Seifert, Cochairs

LETTER FROM THE COCHAIRS

Our original NACD Blue Ribbon Commission report was written in 2012 with the hopes of its recommendations quickly becoming obsolete. Although progress has been made to diversify the composition of the American boardroom, the report's ultimate aspiration has yet to be fully achieved. Recent developments have reinforced the importance of board diversity as a business and societal imperative. The pandemic and widespread protests in the pursuit of racial justice have underlined the significance of building diverse and inclusive boards that can help their organizations to navigate through crisis and drive stronger interconnectedness between companies and the world in which they operate. The demands of this new environment compelled us to refresh our 2012 guidance and issue a new iteration of our mandate on board diversity.

Environmental, social, and governance (ESG) concerns have grown in importance in recent years. Societal pressures, investor expectations, and stakeholder attention have aligned to bring board oversight of diversity to the forefront of conversations on the S of ESG. Recent legislation and regulations on human capital and diversity have created new standards, with many more expected in the next few years. It is imperative, then, that directors consider how their own composition aligns with the gender, racial, and ethnic makeup of their management teams, workforce, and customers. The demand and expectation for diversity on boards will only continue to grow.

Board diversity comes with clear advantages. Diversity of director identity can help boards to understand the needs of their employees, their critical stakeholders, and their consumer base.

Having a diverse board also ensures a diversity of thought and experience, enhancing the collective wisdom and skill sets of the collective board. It is more essential than ever that boards comprise a diverse group of directors with various backgrounds and perspectives in order to perform as effectively as they possibly can. Being a laggard on this issue is no longer acceptable.

NACD's 2019 Blue Ribbon Commission Report makes the case that board leaders must catalyze and orchestrate a transformation in how the board is composed and structured, how it operates and interacts with the business, and how it holds itself accountable. They must unleash the full potential of every director, create an environment that enables diverse voices to be heard, and make uncomfortable decisions about board members who are no longer adding value. In other words, board diversity is now a critical ingredient for building fit-for-future boards.

This is, by definition, not an easy process. The report will discuss the current state of boardroom composition, suggest best practices to increase diversity on boards, and provide solutions to common challenges in diversifying the boardroom. It asks boards to consider if the board itself is representative, having directors with the appropriate skill sets—and challenges them to start having candid conversations about diversity on the board and what prevailing biases may hold back any significant changes.

As chairs of the original commission, we have continued to encourage this report's message for much of the last decade. And we have tried to "walk the walk," advocating for a diverse workforce and board in our organizations.

THE DIVERSITY MANDATE

With increased interest in diversity stemming from investors, stakeholders, and regulators alike, the need for diverse voices in all aspects of a corporation has become critical. Boards do not need to wait to act on this. Boards must lead, and the onus is on them to take up this mandate to unlock the organization's potential and set the tone at the top.

As such, diversity is a moral imperative, as well as a legal mandate in some jurisdictions. At the same time, diversity is a strategic imperative. A high-performing board is one that has a holistic understanding of its organization and its industry. This involves understanding every stakeholder, shareholder, consumer, supplier, contractor, and more. Put simply: corporations will not be able to build or maintain a successful enterprise that yields sustainable long-term stakeholder value without bringing a greater variety of perspectives into the boardroom.

Boards can and should proactively use board agenda-setting to ensure that conversations on diversity and human capital are addressed in every board meeting. Metrics will be key to understanding where the corporation is now, how it is progressing,

and where the board may need to dig deeper. While it is beyond the scope of this report, the board needs to hold the CEO accountable for successfully implementing diversity, equity, and inclusion (DE&I) programs; tracking diversity metrics across the organization; and tying diversity to the corporation's broader value set.

As an aid to implementing these recommendations, this report offers a set of practical tools, examples, and case studies that boards can use to improve diversity in their own boardrooms. These tools will help boards understand investor expectations of board diversity, revamp the board refreshment process, provide oversight of the company's DE&I program, evaluate external disclosure, extrapolate learning from the compensation committee on human capital oversight, and provide key considerations for the lead director.

Our expectation is that every board moves from discussing this topic to taking action to drive forward progress on diversity. It is time for those who are responsible for leading to lead and to move from interest to action.

Sincerely,

Curtis Crawford

Cari Dominguez

Bill McCracken

Kathi Seifert

December 2020

EXECUTIVE SUMMARY

This report was refreshed in 2020 from the original version published in 2012 with new data and guidance generated from more recent NACD Blue Ribbon Commissions as sidebars. While the data has been modified, the core teachings and recommended actions remain original to the 2012 report. A set of practical tools has been added in 2020 to help directors to implement the recommended actions of this Blue Ribbon Commission report.

Corporate boards will face a new set of challenges in the years ahead as major economic and social trends transform the way our companies operate. Not only is global competition growing, but here at home we also see shifting demographics, new customer bases, and increased public focus on diversity in the boardroom and broader workforce. How directors handle these changes can determine the success or failure of the companies they serve.

In light of these new developments, this commission believes that boards must strive for diverse composition as a means of strengthening their own ability to make wise and informed decisions. In particular, this requires racial, ethnic, gender identity, sexual orientation, age, and experience diversity among the board to broaden the viewpoints, skills, and backgrounds of the individual board members. This is the essence of board diversity.

But building a diverse board is not always easy. Many boards aspire to be diverse, yet too few are able to achieve it. There are structural, social, and habitual barriers that have been unconsciously erected to prevent boards from obtaining the very best individuals for the board. These barriers are often not easily visible and operate slowly and subtly. The commission's intent is to shed light on these hidden hurdles and provide some practical solutions.

Diversifying the board is not only possible but also a business and moral imperative, and this report highlights some action steps to accomplish it. Through strong and effective leadership coming from within their own ranks, boards should first discuss diversity and recognize any existing barriers, then select and implement the solutions to best address these obstacles, and finally disclose these actions. These are critical steps in setting the tone at the top, but boards must also remember, "Diversity without inclusion is just an illusion."

1. DISCUSS

Candid, in-depth board discussions about critical topics are at the core of the board's contribution to any enterprise. The topic of diversity is no exception.

2. SELECT AND IMPLEMENT SOLUTIONS

Approaches to building a diverse board will vary. There are some actions, however, that this commission considers indispensable in overcoming any barriers. At a minimum, the commission believes that the following four actions should be taken by all boards that face such barriers:

- **Review and evaluate board composition.** Diversity discussions should be rooted in company strategy and board evaluation. A candid exchange of views on both issues is crucial to understanding the board's composition and the company's strategic needs.
- **Expand horizons for seeking candidates.** Boards should consider setting a nominee-slate target for the nominating and governance committee and recruiters.
- **Improve director evaluations.** Board and individual director evaluations must be strengthened to hold the board accountable as an effective oversight body.
- **Preserve, enhance, or consider adding tenure-limiting mechanisms.** Boards should consider selecting the most appropriate tenure-limiting mechanism for their company. Moreover, boards must adhere to the outcome when a tenure-limiting mechanism is triggered even if the director is still an active participant.

3. DISCLOSE

This commission encourages boards to consider going beyond required disclosures to provide shareholders with a thorough explanation of their director search process and the potential value it brings to the company.

Diversifying the board may take many shapes, but it is more involved than simply adding more women or directors who are from various age groups or candidates who are racially or ethnically diverse or have diverse sexual orientations or gender identities to the mix. Directors must approach the improvement of their board methodically, with the intent of finding the very best talent to complement the company's strategy and needs.

CHAPTER 1 THE POWER OF DIVERSITY

Boards have a fundamental responsibility to advise senior executives and oversee their work. Having a diverse board can help in both respects, as a well-informed and thoughtful group of individuals can provide varying perspectives to decision makers. Such an approach has gained traction in recent years as an antidote to “groupthink.”

With today’s more active and accountable boards, a rich discussion driven in part by diversity is necessary to be optimally effective. This shift away from homogeneity has become a characteristic of forward-thinking companies.

The rising importance of board diversity has coincided with an increase in the complexity and velocity of business. With the growth of large multinational corporations came more rigorous corporate activities to generate shareholder investment. After several major corporate collapses, a greater emphasis was placed on the role of the board. Today, directors are firmly in the spotlight, and shareholder activism—strengthened by growth in institutional holdings—has reached new heights.

Societal changes have also played a major role in corporate governance since the “traditional” board—those with little to no diversity—was the norm. Women now represent a greater portion of the workforce, and the American populace is more racially and ethnically diverse. Successful corporations have adjusted their internal and external business practices to stay competitive in this evolving landscape.

Despite progress on many fronts, some boards remain stuck in neutral—resulting in composition that lacks racial, ethnic, gender identity, sexual orientation, age, or experience diversity. Board searches, for example, have relied heavily on personal networking and word of mouth. This strategy of recruiting within networks, while protecting the board from exposure to unfamiliar

and seemingly “riskier” directors, has led to the unintentional exclusion of many viable director candidates. In short, corporate boards have failed to change with the times.

Looking ahead, a company’s ability to remain competitive will rely on its understanding of global markets, changing demographics, and customer expectations. Diversity is a business imperative, not just a social issue. The new business landscape will require boards to cast a wider net to find the very best talent available. As a natural corollary, the board’s mix of gender, ethnicity, and experiences will likely increase.

Boards now have a choice: maintain the current course and risk being left behind, or restructure board composition and operate at peak performance. The challenge is to not only recognize but also use a much wider pool of talent, which can play a significant and powerful role in corporate governance. While business acumen will always be a necessary skill set for directors, the board’s composition must now also reflect the environment in which the company operates. This process is a cornerstone of a “strategy of inclusion.” This strategy and the suggested methods for achieving it will be discussed later in this report. First, it is worthwhile to understand the current environment of board composition.

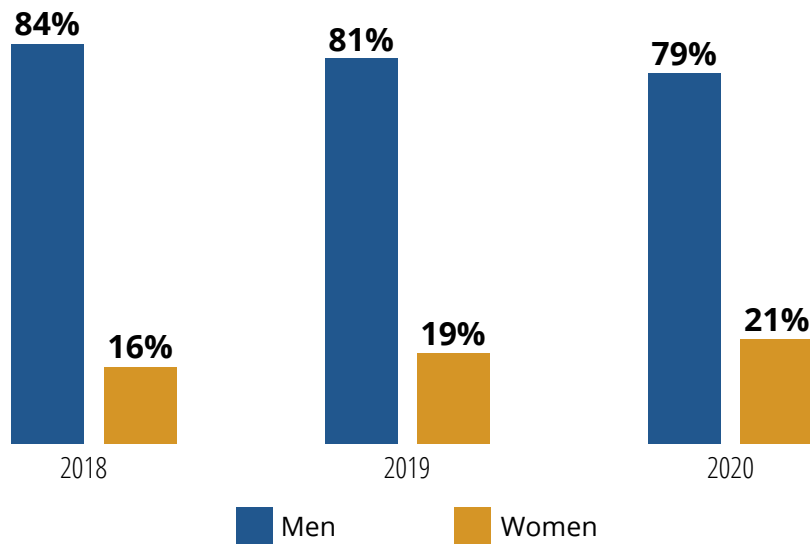
THE CURRENT ENVIRONMENT

Every board operates in its own unique way; the manner in which it approaches diversity is no exception. While some boards could be considered diverse, others have much room for improvement. The surprising fact is that many boards still possess little to no gender, racial, or ethnic diversity.

According to NACD’s *Inside the Public Company Boardroom*,¹ the average board has about 10 members. Gender and ethnic diversity on these boards, however, remains fairly limited.

¹ *Inside the Public Company Boardroom* (Arlington, VA: NACD, October 30, 2020), p. 4.

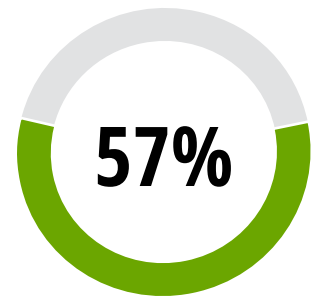
FIGURE 1 PERCENTAGE OF WOMEN ON RUSSELL 3000 BOARDS



Source: *Inside the Public Company Boardroom* (Arlington, VA: NACD, October 30, 2020) p. 6.

Figure 1 shows the percentage of public companies with women directors, which grew from 16 percent in 2018 to 21 percent in 2020.

Racially or ethnically diverse directors have not yet attained the same representation as women: Spencer Stuart reported in 2019 that 23 percent of S&P 500 directors were minorities, defined as African American/Black, Asian, and Hispanic/Latino. Minority women represented 10 percent of the incoming class, up slightly from 9 percent the previous year. Minority men represented 13 percent of the new directors, an increase from 10 percent in 2018—but lower than 14 percent in 2017.²

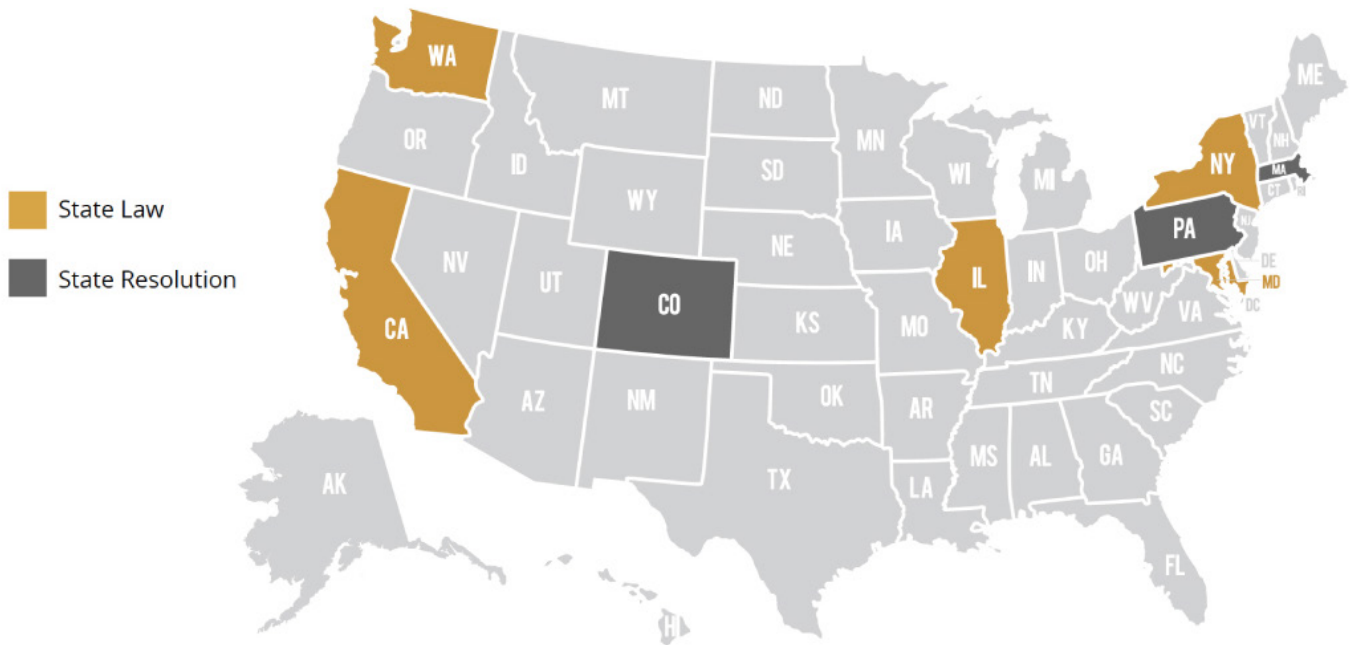


Serving on their first public company board

Source: *Inside the Public Company Boardroom* (Arlington, VA: NACD, October 30, 2020) p. 11.

² 2019 U.S. Spencer Stuart Board Index Highlights (Spencer Stuart, 2019) p. 1.

FIGURE 2 ROUNDUP OF STATE DIVERSITY LAWS AND RESOLUTIONS



Source: *Washington State's New Gender Quota for Boards Reflects Broader Trends* (Arlington, VA: NACD, July 23, 2020) p. 3.

DIVERSITY AS A BUSINESS IMPERATIVE

Diversity of human capital is an accepted business value today. The business need for diversity is evident in the rapidly changing demographic profile of the United States, as well as the continuing rise in the purchasing power of women and various ethnic and racial groups. If not already recognized, businesses and boardrooms will need to be prepared for this shift. Diversity creates positive results for the company, including improved competitiveness and talent management, greater access to capital, more sustainable profits, and better relationships with stakeholders.

In 2020, California passed a bill creating diversity quotas. The bill mandates the inclusion of directors from an “under-represented community” on the

boards of California companies.³ Many other states have diversity laws or regulations in place for increasing board diversity.

There is another factor pushing American companies to increase diversity—the implications of the global marketplace. With today’s global impact on a US company with respect to supply chains, markets, political and economic developments, customers, human capital, and so on, it is increasingly important that a board looks for individuals with business experiences beyond the US border.

³ An Act to Amend Section 301.3 of, and to Add Sections 301.4 and 2115.6 to, the Corporations Code, Relating to Corporations, California State Assembly Bill No. 979, Chapter 316 (2020).

DEFINING DIVERSITY

The act of defining “diversity” is not something to take lightly. In 2019, the US Securities and Exchange Commission (SEC) published new guidance on board diversity disclosure. The new guidance focuses on including a discussion of why “each director or nominee’s experience, qualifications, attributes or skills led the board to conclude that such person should serve as a director of the company.”⁴ It also expects that the board will disclose “a discussion of how the company considers the self-identified diversity attributes of nominees as well as any other qualifications its diversity policy takes into account, such as diverse work experiences, military service, or socio-economic or demographic characteristics.”⁵

The SEC’s approach highlights the difficulty in articulating what diversity means for every company. Proponents of diversity often use one of two descriptions: identity—gender, race, ethnicity—or skills, such as professional experience. Those who champion identity diversity advocate for greater inclusion of women and racially or ethnically diverse individuals in the boardroom. Their argument is that increasing the representation of such diverse candidates will necessarily result in more diverse opinions, perspectives, and skills in the boardroom. Those who favor skills-based diversity hold that boards need to focus on an individual’s skills and experiences as they relate to corporate strategy.

A comprehensive definition of diversity must include both fundamental aspects—identity and skills. Given the nature of the business world today, neither aspect can be excluded. Therefore, a flexible approach is required so that each company can select a unique meaning of diversity based on its needs.

See [page 59](#) for a deeper dive into the boards role in workforce DE&I strategy.

Key Questions Directors Should Ask Themselves

- How does this board define diversity? Does our definition include gender and race/ethnicity?
- If not, why not? Do we wish to change our definition of diversity?
- What type of perspectives or backgrounds will help in the formulation and fulfillment of strategic objectives?
- Does our company value diversity as a means of enhancing competitiveness?

⁴ “Regulation S-K: Questions and Answers of General Applicability: Question 116.11,” US Securities and Exchange Commission, last updated September 21, 2020.

⁵ “Regulation S-K: Questions and Answers of General Applicability: Question 133.13,” US Securities and Exchange Commission, last updated September 21, 2020.

IDENTIFYING NEEDS

Before a board begins recruiting directors, it must first consider its needs in relation to the company's specific characteristics. A regional US bank, for example, will need a different set of directors than an international oil and gas company. These differences are based on each company's profile, including its respective market, strategy, customers, vendors, investors, and employees.

A thorough examination of these factors may identify an area where the board needs additional expertise or perspective. The identification process also includes an internal analysis of the skills and experiences of the current board members. Proper oversight relies on a broad collection of professional backgrounds to understand an enterprise's operations and marketplace. As such, a board should not place all of its recruiting efforts on those individuals with leadership or financial experience. Other candidates with backgrounds in information technology, marketing, or international business may serve effectively on future boards.

See [page 28](#) for recruitment best practices.

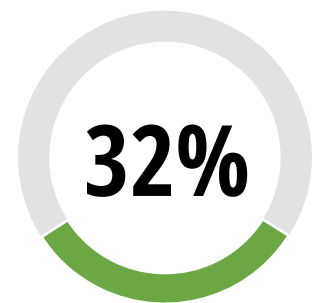
2019 Blue Ribbon Commission Viewpoint⁶

NACD's 2019 Blue Ribbon Commission Report, *Fit for the Future*, discussed the need to continually reassess the board's skills against company strategy. Relevant portions of the report have been added through the publication:

Board diversity—in all senses, from ethnic, racial, and gender diversity to the cognitive and experiential dimensions—is becoming a strategic and moral imperative, as Commissioners in our 2018 report on disruptive risks emphasized. NACD's 2018 public company governance survey reports that 53 percent of companies now have adopted an explicit goal to diversify their board composition.⁷

As a result of the 2020 crises, many directors note that they will reflect on a board set of skills when conducting board refreshment moving forward. Additionally, 27 percent of US respondents to a 2020 survey noted that they plan to set board diversity goals.⁸

What Boards Will Do Differently Moving Forward



Reflect a broader set of skills on the board through board refreshment

Source: NACD, from the upcoming *American Board Practices and Oversight Report*

⁶ NACD, *Fit for the Future: An Urgent Imperative for Board Leadership* (Arlington, VA: NACD, 2019).

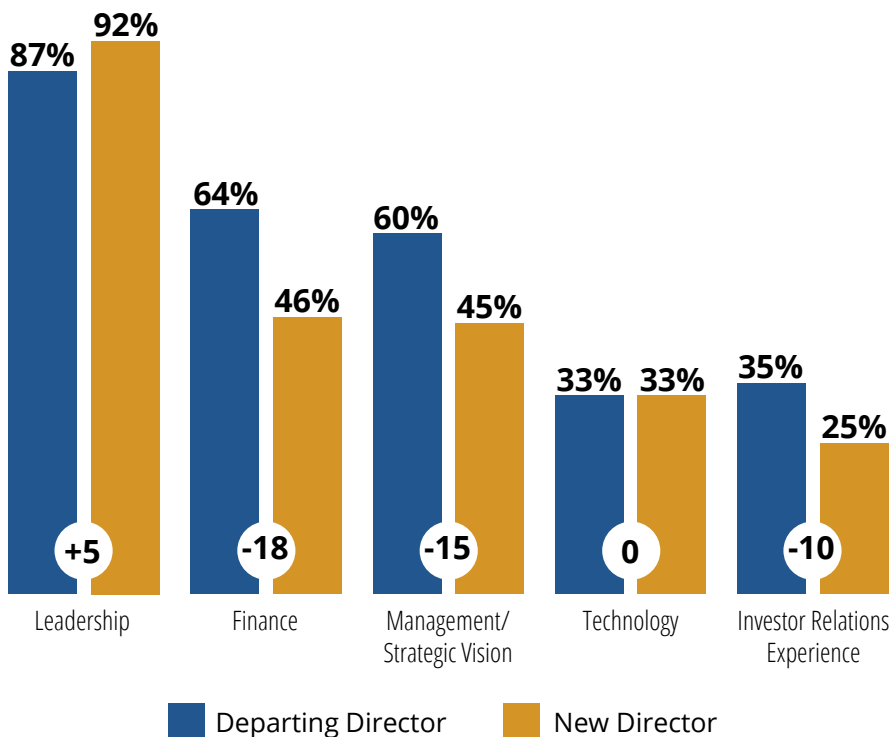
⁷ *2018–2019 NACD Public Company Governance Survey* (Arlington, VA: NACD, 2018), p. 29.

⁸ NACD, from the upcoming *American Board Practices and Oversight Report* (Arlington, VA: NACD, 2021)

RECRUITING FOR VALUE

It is critical to avoid “tokenism” in the selection of new directors. Directors should not be selected solely on the basis of identity diversity. Foremost, a director should be selected for the value he or she can bring to boardroom discussions and decision making. Therefore, the consideration of a candidate’s identity diversity has to coincide with a determination that the individual possesses skills and experiences desirable for the board. This multidimensional approach avoids placing excessive weight on a candidate’s identity, but still incorporates that attribute as part of a full appreciation of all that he or she can bring to the table.

FIGURE 3 NEW DIRECTORS AND DEPARTING DIRECTORS POSSESS DIFFERENT SKILL SETS



Source: *Inside the Public Company Boardroom* (Arlington, VA: NACD, October 30, 2020) p. 12.

2019 Blue Ribbon Commission Viewpoint

As discussed during the 2019 Blue Ribbon Commission meetings, the board leader and the chair of the nominating and governance committee should thoroughly assess whether the board has the right human capital to fulfill its mandate and deliver ongoing value. One of the key questions will be whether the board’s existing composition is aligned with the challenges likely to face the business in the future sketched out together with the management team, and if not, how it should best be renewed. One useful way of thinking about this task could be a “clean-sheet” approach to board diversity and composition, which NACD first recommended in its Blue Ribbon Commission report on building the strategic-asset board. In particular, nominating and governance committees should consider asking the following questions:⁹

- If we were to create a board from scratch today, what would it look like holistically, from the standpoint of skills, leadership styles, and backgrounds? What will we need in three, five, or more years?
- Have we sufficiently mapped out our strategy and risks into the future to understand what profiles we need?
- How should our board composition represent the characteristics of the company’s current and future customer base as well as its workforce?
- If we are anticipating adding one or more new directors in the next couple of years, have we vetted our recruitment profile to ensure criteria are relevant and that they are not unnecessarily restricting access to appropriate candidates (e.g., requiring CEO or prior board experience)?

⁹ *Fit for the Future: An Urgent Imperative for Board Leadership* (Arlington, VA: NACD, 2019), p. 23–24.

CHAPTER 2 A STRATEGY OF INCLUSION

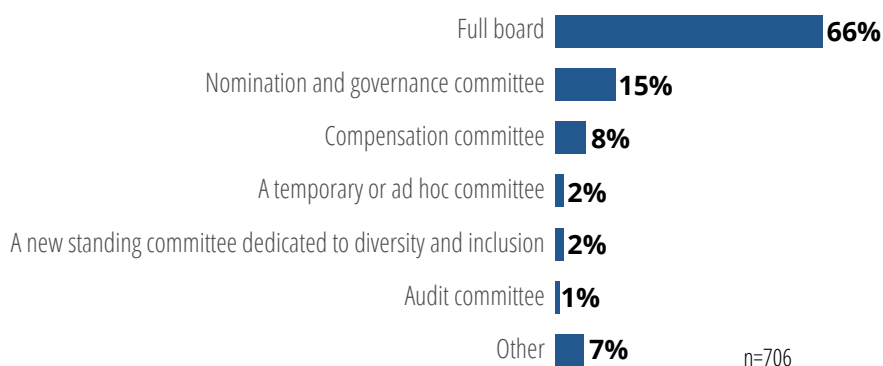
Most boards today are ready and able to move past barriers to achieve greater diversity in the pursuit of excellence. Yet, in many cases, identifying the impediments and implementing solutions can be difficult. The job of advancing diversity is a challenge that requires strategy and leadership.

This chapter will provide the building blocks of a strategy, outlining the necessary steps for enabling change. In brief, the steps are to discuss diversity and recognize any existing barriers, select and implement the solutions to best match these obstacles, and disclose these actions. But a strategy alone is insufficient; strong leadership will be required to see it through. On each board, someone must be willing to step up, start the conversation, and ask the difficult questions. For the benefit of the organization, the board must be willing to push for the implementation of the following three steps.

1. DISCUSS

Candid, in-depth discussions among all the directors about critical topics are at the core of the board contribution to any enterprise. The topic of diversity is no exception. Though committees can play a key role in improving diversity, all members of the board have a shared responsibility to discuss the topic in full.

FIGURE 4 WHERE OVERSIGHT OF ORGANIZATION-WIDE DIVERSITY, EQUITY, AND INCLUSION IS LOCATED



Source: NACD, from the upcoming *America Board Practices and Oversight Report*

Learn key lessons from the compensation committee's oversight on culture to inform board oversight on [page 40](#).

2019 Blue Ribbon Commission Viewpoint

The board leader has a critical role to play in activating diversity in the boardroom by recognizing that the aim is not “hiring for diversity and then managing for assimilation.” With higher levels of diversity in the boardroom—whether this is diversity in experience, skills, gender, race, ethnicity, or age—it's critical for board leaders to create a culture that facilitates constructive and candid interactions between board members and that ensures that each director is heard from on important issues.¹⁰

¹⁰ *Fit for the Future: An Urgent Imperative for Board Leadership* (Arlington, VA: NACD, 2019), p. 25.

Ensuring diverse viewpoints in the boardroom is a perennial task. Ideally, a discussion on director composition would follow the yearly board evaluation and succession planning. The findings from the review can provide a good starting point for addressing the skill sets and perspectives of board members. Therefore, evaluations should include a question regarding whether the board is sufficiently diverse as defined by the company. Placing a diversity question into the annual board evaluation allows the facilitator to expose this issue and skillfully place it for board discussion.

2. SELECT AND IMPLEMENT SOLUTIONS

In Chapter 3 of this report, the commission identifies a variety of tactics to overcome the potential barriers to diversity. A board cannot, however, implement all the solutions at once. Attempting to do so would likely prove unwieldy and inefficient. Instead, boards should assess the barriers they face and then select the solutions for improvement.

There are some actions, however, that the commission considers indispensable in overcoming the structural, social, and habitual barriers described in Chapter 3. At a minimum, all boards should take the following four actions:

- *Review and evaluate board composition.* Diversity discussions should be rooted in company strategy and board evaluation. A candid exchange of views in both areas is crucial to understanding the board's composition and the company's strategic needs. This discussion may also include a critical analysis of the roadblocks that stand in the way of the board's path to diversity—as the board defines this term.
- *Expand horizons for seeking candidates.* Boards should consider setting an expected "target" for nominee slates for the nominating and governance committee and recruiters.

For example, if a board determines that women are underrepresented, the nominating and governance committee could ask its recruiter(s) to deliver a slate with half of the candidates being women. Another option may be to work with multiple recruiters to ensure the identification of a broader pool of talent.

- *Improve director evaluations.* Board and individual director evaluations must be strengthened to hold the board accountable as an effective oversight body. Evaluations should be designed with the intention of improving director performance. Where an individual is underperforming, mentoring and education may be appropriate. If an individual consistently underperforms or has unnecessary skill sets, the board should not renominate the director.
- *Preserve, enhance, or consider adding tenure-limiting mechanisms.* A key element to improving board diversity is to increase director turnover. Usually, boards are most effective when fresh and independent perspectives are routinely added over time. Therefore, boards should consider selecting the most appropriate tenure-limiting mechanism for their company. Moreover, boards must adhere to the outcome when a tenure-limiting mechanism is triggered, even if the director is still an active participant in the company's strategic needs. This discussion may also include a critical analysis of the roadblocks that stand in the way of the board's path to diversity—as the board defines this term.

Understand the board leader's unique role in driving diversity on [page 31](#).

3. DISCLOSE

SEC regulations require a board to disclose whether—and, if so, how—a board considers diversity during a candidate search.¹¹ This commission encourages boards to consider going *beyond* what is required: provide a thorough explanation of the search process and the potential value it brings to the company's operations. The proxy statement can be used to refresh stakeholders' knowledge about the company's policies, philosophy, and accomplishments on diversity. Most importantly, the message should be clear: the board sought the most qualified directors possible from a broad pool of candidates.

Learn how other companies are measuring, setting goals on, and reporting on diversity, equity, and inclusion on [page 52](#).

Board Disclosure on Diversity

Communicating the board's diversity focus and policies to shareholders is critical. Consider the following practices when creating your disclosure:

- Think outside the traditional skills box. Include business experience and skills that directly relate to the company strategy.
- Explicitly disclose the board's diversity considerations and criteria for director nominees.
- Disclose who owns diversity oversight and how that committee oversees it.
- Communicate the role diversity plays in the board evaluation and refreshment process.

¹¹ US Securities and Exchange Commission, [Proxy Disclosure Enhancements](#), Release Nos. 33-9089 & 34-61175, Dec. 16, 2009.

CHAPTER 3 BARRIERS AND TACTICS FOR IMPROVEMENT

Many boards aspire to be diverse, yet too few are able to achieve it. The barriers to achieving diversity—deeply ingrained structural, social, and habitual factors that operate slowly and subtly—are often not easily visible. The commission’s intention is to shed light on these hidden hurdles and provide some possible solutions.

The following chapter is organized according to these three types of factors. In many cases, barriers may be both structural and behavioral. Similarly, the possible solutions may address more than one problem. For the following sections, this commission is aware that not all boards need to implement all of the solutions. Some boards have identified their own specific barriers and have begun to apply corrective measures; others have made much less progress.

STRUCTURAL FACTORS

Unfortunately, some of the processes boards have relied on for decades inhibit the creation of dynamic, diverse boards. Many common board features, such as the absence of any type of tenure-limiting mechanism, have led to unintended consequences.

Absence of Tenure-Limiting Mechanisms, Such as Term Limits

Ten percent of boards have term limits.¹² Of those that do, some are willing to bypass the limiting provisions to allow a director to serve for a longer period. These factors have decreased director turnover and prevented fresh perspectives from entering the boardroom.

The world of politics offers an interesting analogy on term limits and incumbency. In the political arena, it is often argued that term limits are unnecessary, as politicians can be voted out of office at the next election. In reality, the power of incumbency is substantial and has led to many extended careers in politics. Similarly, boards cite shareholder voting as the instrument to force director turnover. Moreover, boards themselves struggle to address the underperformance of individual directors. In a recent survey, 46 percent of directors agreed that designated board leaders fail to remove directors who are no longer qualified to serve.¹³

Five Steps for Effective Offboarding¹⁴

- 1. Set expectations at the outset.** Incorporate the idea of off-boarding early on, as soon as a director interviews and then starts on to the board. This can help normalize leaving the board and reduce any associated stigma.
- 2. Make conversations about performance and the company’s needs a regular occurrence.** When done correctly, conversations about off-boarding should then come naturally and be less contentious given the ongoing and open nature of the performance dialogue.
- 3. Make the most of the board evaluation process.** A true evaluation is seen as a performance tool rather than a “check-the-box” exercise and can help identify underperforming directors.
- 4. Ensure that the nominating and governance chair and the full-board leader guide the process together.** Who leads the discussion with a director designated for off-boarding will differ depending on the board’s culture and the role of the director being asked to leave.
- 5. Create a pathway for engagement post-directorship.** Directors who have been with the company for a long period of time may have valuable insights to share with current and new directors through a director emeritus program.

¹² *2018–2019 NACD Public Company Survey*, (Arlington, VA: NACD), p. 59.

¹³ *Fit for the Future: An Urgent Imperative for Board Leadership* (Arlington, VA: NACD, 2019), p. 17.

¹⁴ *The Healthy Departure: Considerations for Effective Off-Boarding* (Arlington, VA: NACD, 2020).

SOLUTION Preserve, Enhance, or Consider Adding Mechanisms to Increase Director Turnover

In general, this commission believes that more frequent turnover is beneficial to the board. However, currently, more than 55 percent of boards do not replace a single director during the course of one year.¹⁵ Boards should use the tools already available to increase turnover, such as term limits, age limits, or resignation requirements upon change in job status. All of these mechanisms need not be used at the same time; rather, directors should select the most appropriate methods of turnover for their board.

Careful consideration of tenure-limiting mechanisms is crucial. Age limits, for example, may not be right for all boards, as older directors can bring valuable experience; this could, however, open up the possibility of a lack of age diversity. The commission believes that the goal should be to work toward more diverse boards while carefully maintaining good governance.

Small Board Sizes

Corporate bylaws typically spell out a range for board size—generally from five to 15 directors. For reasons of effectiveness, cost, and group dynamics, public company boards rarely exceed a dozen members. Subsequently, a lack of available board seats has often been cited as a reason for little or no director diversity—there just isn't room to add diverse directors.

SOLUTION Consider Temporarily Expanding the Board's Size

When a board knows in advance of an upcoming retirement, it can temporarily add new directors before the retirement occurs. These new directors will continue to serve after the retiring director has left, and the board will contract to its original size. A temporary increase in size allows for the inclusion of directors of

diverse backgrounds without threatening the seats held by current directors. This practice may also help transfer institutional knowledge through the overlap of board members

Inadequate Use of Evaluations as a Tool For Board Turnover

Evaluations are an opportunity for boards to review their current composition and make changes reflecting current needs in relation to the corporate strategy. Concurrently, an evaluation can identify those individuals not contributing to company value. The results from board evaluations, however, are not always robust; at times, there may be a natural tendency to preserve the status quo. Effectively used, evaluations are a valuable tool for assessing board members' performance, boardroom composition, and gaps in skill sets.

SOLUTION Give Evaluations Traction

Evaluations primarily enable a board to gauge performance and make adjustments consistent with the company's strategic direction. Improving this process only occurs when evaluations are also used as a tool for director accountability. Evaluations, and in particular individual director evaluations, should be designed to improve performance. However, a director's consistently subpar performance warrants decisive board action. In these cases, the board should act on the evaluation results and lay out a performance improvement plan. If that fails to achieve the desired results, it may be necessary for the board to take action and either ask the director to resign or not nominate the director for reelection.

Third-party board evaluations may help make the evaluation process easier and more effective. Evaluation comments tend to be more candid and instructive when independent outside consultants are used. This way, board members may avoid potential social drawbacks but still retain evaluation effectiveness.

¹⁵ Data and company intelligence collected from **MYLOGIQ** - 360° Public Company Intelligence, www.mylogiq.com, and Russell 3000 (as of November 23, 2020), NACD analysis.

Inadequate Use of Executive Talent Management to Develop Directors From Within

Many current executive talent management programs do not yet effectively prepare individuals with diverse backgrounds for the boardroom. While talent programs do and should have a management focus, exposure to boardrooms may still be limited.

SOLUTION Enhance Executive Talent Management Programs to Expand the Pool of Diverse Directors

Specifically, training programs could educate young executives on boards' roles and responsibilities. Additionally, executives should be encouraged to serve on outside company boards as well as nonprofit boards. Current CEOs could help pave the way for these individuals by making the necessary introductions and personal connections. Additionally, continuing education classes could familiarize the executives with board operations. If implemented, this approach could potentially increase the overall pool of director candidates, as well as expose the individuals to a broader view of the business world. This would only enhance their performance at their current positions.

SOCIAL FACTORS

Certain inherent social behaviors apply to every individual, regardless of race or gender. For example, individuals will often prefer or relate to people who are similar to them.¹⁶ These basic human behaviors are, in part, determining the outcome of boardroom composition.

Little Knowledge of Where to Find Candidates

A current recruitment style of identifying new candidates through word of mouth may encourage sitting directors to select those they know without reaching outside their personal networks. For example, boards may ask, "Who do we know?" as the first step in a director search, and the resulting candidates may come from similar social circles, geographical locations, or professional relationships. This selection style, therefore, is prone to perpetuating the status quo on board composition.

Use Board Evaluations to Think Like an Activist

Outside of informal feedback, evaluations can be a tool that helps directors to recognize board members who may be falling behind on expectations—they may even help a board member to self-identify as a director whose ability to contribute to the board is waning. A true evaluation is seen as a performance tool rather than a "check-the-box" exercise. Evaluations are a natural way to signal to the nominating and governance chair that it is time for the director to leave.

These evaluations can also serve as a report card for the board when running tabletop exercises of an activist attack. Ask yourself, if an activist shareholder demanded changes to the board tomorrow, who would they select for off-boarding—and why? The answers can be used either to strengthen directors' skills or as a platform for the off-boarding discussion and decision.¹⁶

¹⁶ J. Philippe Rushton and Trudy Ann Bons, "Mate Choice and Friendship in Twins: Evidence for Genetic Similarity," *Psychological Science* 16, no. 7 (2005): 555-59.

¹⁷ *The Healthy Departure: Considerations for Effective Offboarding* (Arlington, VA: NACD, 2020), p. 3.

Knowledge of an individual is also an issue for search firm candidates. Because boards will generally prefer a candidate if they have had some previous positive contact, a search firm's candidate may subsequently face an uphill battle if he or she lies outside the sitting directors' personal networks.

SOLUTION Expand Horizons When Seeking Candidates

Rather than making general statements about diversity, nominating and governance committees should establish an expected "target" for nominee slates presented by recruiters—for example, no less than one-third of candidates for new board seats should match the board's definition of diverse. If the diverse candidates on the slate are not appropriate for addition to the board, then the committee must insist that the recruiter cast a wider net for talent.

Additionally, just as audit and compensation committee members are encouraged to attend outside training to stay current, members of nominating and governance committees could be encouraged to network with potential directors. NACD and other organizations offer many opportunities for committee members to look beyond their current horizons.

Overboarding of Certain "Star" Board Members

Regardless of gender or ethnicity, director searches often turn up with the same directors' names time and time again. Boards and recruiters frequently work with the people they "know"—most often, proven directors who currently serve on other boards. Thus, the pool of diverse talent on boards is not expanded, just recycled from board to board.

Unfortunately, the director world is already small; the added requirement for diverse membership further limits the field. Naturally, certain diverse

directors are sought after because they are high-performing individuals. While the commission does not object to proficient directors taking on a greater number of board seats, this does raise a concern about time commitment. The possibility of overboarding can decrease the effectiveness of these directors, and 38 percent of the Russell 3000 have an active overboarding policy for directors.¹⁸

SOLUTION Move Beyond the "Star" Diverse Board Members

Go beyond the crowd of known people. Use third-party references or a search firm to identify candidates who, while not already on boards, are otherwise qualified.

Reluctance of Sitting Directors to Leave a Board

Directorships are coveted positions. The prestige, network, and compensation are valuable aspects of a directorship. As such, it can be expected that few directors would voluntarily give up their seats to make room for a diverse director. As boards do not often change composition, a stigma can be associated with being removed from a board—even if it is for a reason entirely unrelated to performance. To avoid this stigma, boards rarely remove directors, thus opening fewer board seats to diverse directors.

SOLUTION Adhere to Term-Limiting Mechanisms to Build Turnover Acceptance

Making turnover routine will help remove much of the stigma of change, as well as bring about more diverse and stronger boards. The use of practices such as term or age limits, when adhered to, can facilitate this process. In some cases, boards may want to designate directors who are rotating off as ex officio or emeritus. This model may allow for a more gradual, easier transition off of a board.

¹⁸ *Inside the Public Company Boardroom* (Arlington, VA: NACD, 2020), p. 23.

Consolidating Diversity Into One Category and Related Stereotyping

When categorizing all racial and ethnic groups together as “minorities,” boards miss a chance to find the best candidates for their companies. Essentially, diversity means openness to all candidates. Is a board with women but no racial diversity, or vice versa, sufficiently diverse? By adding two Hispanic directors to a board, will the nominating committee believe the “diversity job” is done and miss a good skills match with the next candidate?

SOLUTION Do Not “Check the Box”

Do not assume that once you have one woman and one person of color that your quest for an optimally qualified, diverse board is accomplished. Remain open to a variety of candidates—including those who correlate to your customer base. Above all, avoid developing a quota mentality; instead, search for excellence in performance.

HABITUAL FACTORS

Habits are one aspect of human behavior that proves particularly difficult to change. Generally, people adhere to routines and often resist attempts to deviate from them. In the boardroom, extending this practice to composition can decrease its effectiveness. The following illustrates some of the habits hindering board diversity.

Failure to Put Diversity on the Board’s Agenda as a Discussion Topic

Too often, diversity is perceived as an issue of compliance rather than strategy. Also, some directors may be hesitant to bring up an issue seen as “too political.” In other cases, directors have experienced difficult board conversations about the issue and hesitate to bring it up again.

SOLUTION Place Diversity on the Board’s Agenda as a Topic for Discussion and Education

Diversity should be a continuing topic of discussion on the boardroom agenda. For productive dialogue, it is imperative that directors are not reluctant or fearful to speak on the topic. Chief executives should also share the responsibility for putting diversity on the agenda if board members fail to act. Only 27 percent of directors surveyed in 2020 said they set board diversity goals.¹⁹

¹⁹ NACD, from the upcoming *America Board Practices and Oversight Report* (Arlington, VA: NACD, 2021)

Tendency to Seek Only CEOs and Experienced Public Company Directors for Board Seats

Generally, CEOs are the most highly sought for board openings. By limiting the search to CEOs, boards miss out on many other aspects of diversity—race, ethnicity, gender identity, sexual orientation, age, and professional background or experience.

SOLUTION Move Beyond CEOs in Seeking to Fill Board Seats

Searches can be extended to include those who do not yet serve on a board but have the qualifications to become successful directors. This list could include entrepreneurs, rising high-performance executives with profit & loss (P&L) responsibility, nonprofit leaders, prominent investors, and a variety of other individuals whose expertise can benefit a board on an ongoing basis.

Existing Lack of Diversity on the Nominating and Governance Committee

In recent years, the nominating and governance committee has become increasingly responsible for pursuing new director candidates. Committee composition, however, has largely not been a principal issue for most boards. If the committee composition reflects a narrow perspective, new director searches may be limited.

SOLUTION Diversify the Nominating and Governance Committee

Committee members can exert a great amount of influence on the director selection process. Just as independence breeds independence, a diverse committee can play a significant role in increasing diversity on the board. At a minimum, nominating and governance committee members should encourage greater participation from diverse directors during the search for and selection of candidates.

CHAPTER 4 BEYOND THE BOARDROOM: INTO ACTION

Boards play a unique and important role in moving toward diversity, but they cannot do it alone. Candidates, recruiters, and investors also play a part.

WHAT THE DIVERSE CANDIDATE OR NEW DIRECTOR CAN DO

Boards will be unable to find the diverse talent they need without action on the part of each potential director. These recommendations may seem self-evident, but their importance warrants a brief mention.

Devote time to networking and education.

As mentioned earlier, directors are still found predominantly through personal networks, although there are equally effective recruitment measures to find diverse directors. Sitting directors will typically look for individuals they know to fit the role. Therefore, those seeking director positions can increase their own visibility and improve their understanding of board work by participating in educational events, governance sessions, and conferences.

Understand boardroom dynamics. Board newcomers often do not fully understand the dynamics of a boardroom until they have obtained a directorship. Transitioning from a management role to an oversight role can be a challenge. There are new skills to learn, including active listening and the ability to articulate a position diverging from those of others.

Learn to influence without being the leader.

New directors are often elected to a board after spending a considerable amount of time in a position of operational leadership, and the transition from management to oversight can be difficult. In most cases, a new director will not be assigned as chair or lead director. Despite this fact, every director still has a leadership responsibility that

is demonstrated through constructive skepticism, the courage to make tough decisions, and the maintenance of high ethical standards.

WHAT RECRUITERS CAN DO

Recruiters can have an enormous impact on building a diverse board. A firm with experience in board recruiting can be a dispassionate intermediary when conducting the board search and possess the sensitivity needed when introducing, positioning, and socializing the diverse candidate. It is important for recruiters to cast a wider net in bringing more diverse perspectives into the boardroom. Boards tend to look for CEOs and chief financial officers, but there are functional heads who are also broad business thinkers and should be included as part of the candidate pool—this includes those in marketing, human resources, and law.

Executive/director search firms should:

- Work with the nominating and governance committee to create a slate that includes a significant percentage of diverse candidates.
- Demonstrate the importance of searching for suitably diverse individuals to the nominating and governance committee.
- Help boards understand the director succession-planning processes with regard to developing tenure-limiting mechanisms; these allow corporations to reinvigorate the ranks of their boards with individuals with fresh perspectives.
- Go beyond the nominating and governance committee to ensure more open participation by the entire board.

- Educate boards on best practices for candidate recruitment and selection.
- Expand the search for individuals below the C-suite with P&L experience.

While working with recruiting firms, the board's nominating and governance committee should insist on candidates who match their diversity needs. If the presented slates do not feature high-quality diverse candidates, work with the recruiting firm to find more suitable individuals.

WHAT INVESTORS CAN DO

Shareowners, too, can be a significant force in advancing boardroom diversity. Some major institutional investors—for example, the large public pension funds CalPERS and CalSTRS—are already advocating for diversity on corporate boards through shareholder proposals and negotiations with companies where they own shares.

Pro-diversity investors can

- seek to educate other investors about the economic value of diversity,
- prioritize board diversity as an important criterion when choosing companies to invest in, and
- consider being an advocate for diversity not only at the companies they own directly but also at companies with shares traded through major index funds.

Understand diversity initiatives from top investors on [page 47](#).

Board Oversight of DE&I Programs

As discussions around diversity gain momentum in the boardroom, boards need to ask the right questions to provide effective oversight of the DE&I programs at the companies they serve. To create and maintain a diverse corporation, the board should work with the CEO to understand the hiring practices and assumptions, learning and development, and performance metrics that track the company's progress.

To spur their CEOs along, directors should consider the following action items:

- Clearly map out the board's expectations for diversity throughout the organization.
- Make diversity a goal that is tied to the CEO's compensation plan, using quantitative metrics alongside qualitative assessments.
- Consider using employee engagement surveys, along with tracking the demographics of the organization, as a quantitative measure of success on the CEO's DE&I strategies.
- Make DE&I a regular board agenda item, requiring updates on the company's DE&I initiatives and progress made by the CEO and the DE&I team.

See key questions to ask management and red flags to avoid on [page 71](#).

CONCLUSION

After 25 years of little to no change in the demographic traits of US boards, enlightened corporate leaders are recruiting directors with a range of professional backgrounds, skills, experiences, nationalities, and abilities. These changes in composition are not driven by quotas or moral obligation. Rather, the desire for sustainable corporate performance and growth has demanded this evolution.

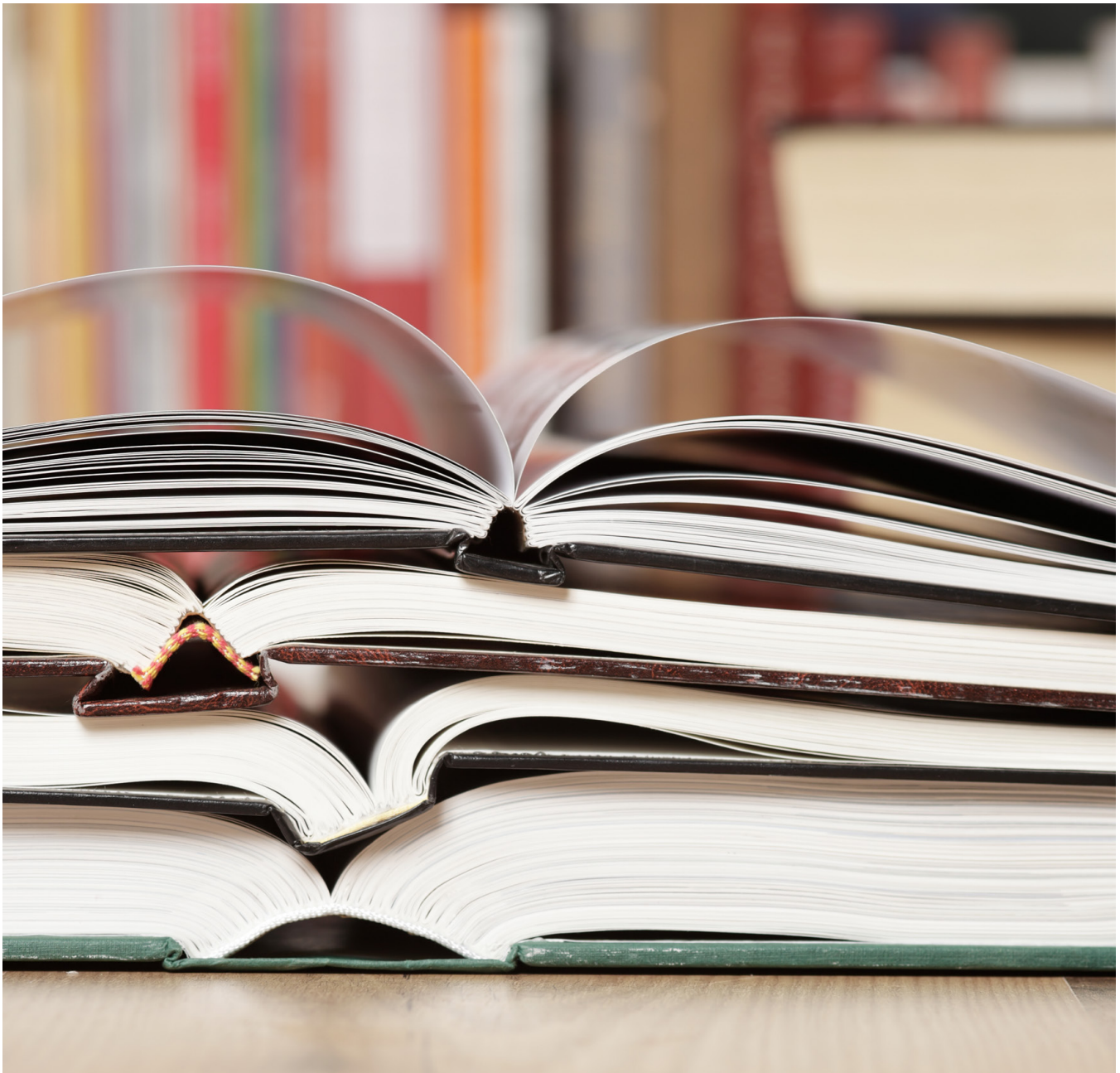
While this commission believes that a diverse boardroom will bring about better discussion, decision making, and critical oversight, some obstacles still impede the achievement of this goal. These obstacles are not insurmountable but will require strong leadership. Where will this leadership come from? As corporate leaders, it is our responsibility to steer our boards and companies in the right direction. The challenge, therefore, is upon each of us.



TOOLKIT MATERIALS

Blue Ribbon Commission Toolkits contain materials that can help directors to implement the report's recommendations (e.g., suggested questions for boards to ask themselves and/or members of management, examples of committee charters, board-level reporting dashboard templates, examples of disclosures, etc.). NACD consistently

receives feedback from directors that these tools significantly enhance the value of Blue Ribbon Commission reports. While the core Blue Ribbon Commission report and its recommendations will be available to the public, access to Toolkit materials is reserved for members of NACD.





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