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# FUTURE ENERGY WORKFORCE: THE ROLE OF CORPORATE BOARDS IN DIVERSITY AND PERFORMANCE

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Corporate boards provide a governance structure for decisions regarding the future direction and objectives of the corporation on behalf of shareholders. It is the board's responsibility to ensure that the company is run efficiently to maximize shareholders' returns. As part of this oversight function, the board approves or sends back for amendment management's recommendations for strategy and examines complex issues such as audit, compensation, and nomination and governance. Management reports to the board about its progress in meeting objectives.

Academic research shows that companies with boards with higher levels of diversity create a richer and deeper conversation around the boardroom, facilitating better monitoring of management, improved innovation of ideas, and ultimately superior performance. Carolyn Wiley and Mireia Monllor-Tormos demonstrate that boards in which women comprise 30 percent or more of the membership achieve higher financial performance in the science, technology, mathematics, and finance sectors—including energy—than firms with less or no diversity.[1] Board diversity expands perspectives and reduces groupthink, creating a positive effect on the board's monitoring functions. This is in contrast with boards where a single female board member may be perceived negatively and treated with distrust or doubt.

In recent years, institutional investors in energy firms—both passive, exchange-traded fund investors such as Vanguard, BlackRock, and State Street as well as active, fundamental investors such as Fidelity, Capital Research, and T. Rowe Price—have successfully engaged energy companies to add women to their boards of directors to enhance performance. The number of shareholder proposals related to board diversity has been rising in recent years, with a sharp acceleration seen in 2019.

Some US states have initiated regulatory actions to require more diversity on corporate boards. For example, in September 2018, then California governor Jerry Brown signed a bill into law that requires publicly traded corporations headquartered in the state to include at least one woman on their boards by the end of 2019 and three women on boards greater than six by the end of 2021. At the time the governor signed the bill, a quarter of California's public boards did not have any women, a situation that was almost completely reversed at the close of 2019. Similar legislation has been proposed in Michigan, New Jersey, and Pennsylvania. But the record on the use of hard targets as a way of achieving board diversity is still under debate as a means to achieve diversity goals. Researchers Kenneth Ahern and Amy Dittmar found that Norway's 2006 hard target of a 40 percent requirement of women on corporate boards of directors led in some cases to younger and less experienced boards, with negative effects on performance.[2] This is in contrast to the same diversity being achieved through voluntary measures within the Fortune 1,000, where enhanced governance and performance were achieved through improved diversity.[3]

## WORKSHOP SUMMARY

The Women in Energy program at Columbia University's Center on Global Energy Policy recently convened a workshop to discuss the role of the board of directors and how a diverse composition affects board deliberations and effectiveness. The workshop addressed the main issues that energy companies are facing at the moment, discussed and highlighted the benefits of having diversity at the top—in both the C-suite and at the board level—and offered solutions and recommendations on how that diversity can be achieved.

Participants included shareholder and corporate advisory experts; academic, finance, and management scholars; business consultants; independent board members of energy companies; leaders from executive search firms; and energy corporate C-suite leadership.

The workshop began with reporting on the current status of diversity on corporate boards in the energy sector, which still lags broader industry in the United States on diverse workforce and leadership. In the first eight months of 2019, the percentage of board seats held in the Russell 3,000 index of companies stood at 20.2 percent overall, whereas women represented 14.9 percent of board seats in the energy sector. Ethnic diversity was lower in both categories: 10.5 percent of seats in the Russell 3,000 could be characterized as ethnically diverse, with only 6.2 percent of seats on energy sector boards. Utilities have fared better at 27 percent of seats held by women and 14 percent of directorships held by ethnic minorities.

The workshop then covered a variety of topics, including promoting inclusive board culture; fostering talent pipelines; the role of environmental, social, and governance (ESG) issues in promoting access to capital; and current business challenges to energy leaders. This workshop report reflects the highlights of the discussion, which was held under Chatham

House Rule. In some instances, the authors have supplemented the highlights with citations to works that provide deeper insights into certain issues.

## Board Culture

Workshop presenters and participants emphasized the importance of corporate culture in fostering the success that can come from diverse boards, leadership, and workforce.

Corporate culture comes from the top. It is typically set by the CEO, who needs to make sure not only that there is agreement among board members but that all voices have been heard and all concerns have been debated. One important aspect of creating diversity on boards is to have everyone contribute toward the achievement of this goal. One cannot expect the new diverse person on the board to produce the "diversity" improvement by themselves, but rather through everyone's interactions.

Do energy boards foster a culture for exchange of ideas and where assumptions can truly be discussed and challenged? This is a very important question, and the energy sector is making progress, albeit from what many investment analysts suggest has traditionally been a relatively low baseline. It was noted that European companies are required by law to have separate chairperson and CEO roles, and this may encourage new approaches to changing energy businesses than their North American counterparts. However, the separation of the chairperson and CEO title alone does not necessarily ensure a better culture for the exchange of ideas.

Research has shown that firms with employees with high satisfaction outperform others on quality, profitability, productivity, and shareholder returns.[4] To develop this kind of positive culture typically involves a visible alignment between a company's purpose and core values and its daily culture, which should be linked to reward systems for employee conduct. Not only should the company's code of conduct be clearly articulated, but accountability must extend from the CEO and top management to the board and all employees. Robust corporate culture requires effective communications processes across the organization as well as externally and exhibit a resilience to changing business realities and competitive pressures.

Small group experiments show executives tend to work harder to hear and listen to comments if they are in a diverse environment. Diversity allows for each participant to think more inclusively about each team member's input. In a homogenous group, there is more personal concern about not rocking the boat by raising a different point of view. Work done by Columbia University professor Katherine Phillips shows that diverse teams actually make better decisions and create better outcomes with the issues they have to solve.[5]

Board evaluation processes can be used to review board working culture to ensure that boards are getting the benefits of diversity. Boards set an example for the company, and as part of their monitoring responsibility, they should be attuned to making sure that what the company says on diversity aligns with what employees are observing and experiencing. To facilitate, boards can offer a written policy on their role related to the culture of the corporation. The National Association of Corporate Directors published a report on corporate culture as an asset in 2017 and noted that directors should review board culture on a regular basis and use board composition and succession planning as an opportunity for continuous improvement. They also recommended the following:[6]

- Directors should make culture an explicit criterion in the selection and evaluation of the CEO and set the expectation that CEO and senior leaders do the same in their own leadership development and succession planning.
- Boards and compensation committees should review recognition and reward systems to ensure they reinforce the desired culture and avoid unintended outcomes that could undermine the culture.
- Boards should set the expectation with management that regular assessments of culture will include both qualitative and quantitative information and incorporate data from sources outside the organization.

## Board Candidate Talent Pipeline

Workshop participants discussed the important challenge of how to build a pipeline of qualified, diverse board candidates. One has to consider whether there is a problem with current selection criteria. How does one view "value" criteria, and are they "male"? Do search firms look for women who resemble men in their work style and behavior? Academic literature argues that such an approach would not create the right diverse dynamics around the boardroom table that would produce the optimum level of the benefits to diversity. The industry also faces the problem of the same women serving on multiple boards instead of having stretch candidates from other backgrounds. Most proxy advisory services have taken note, and advisers such as Institutional Shareholder Services and Glass Lewis are now recommending voting against board members that sit on more than three public boards.

One reasonable path for creating a stronger pipeline of diverse candidates is for companies to promote visibility of their senior women, which would position these women to serve on boards, create powerful professional networks, and forge strong alliances. As a general observation, women are typically underused in firm brand and reputation building. There is a large potential to tap women leaders to attract interest from business media, television, and conference organizers. For example, Bloomberg recently mandated that its employees cannot participate in any panel that does not have at least one woman speaker. Increasing the visibility of women leaders in firms also has the benefit of attracting diverse talent to the firm's overall job pool and helps promote retention of mid-level diversity.

Another aspect that was discussed in depth was the executive search process, both for the C-suite and for the board. The conclusion was that executive search firms do not have a great track record of creating transformational change inside their client companies, diversity and inclusion considerations included, and that ultimately, the relentless drive toward increasing diversity has to come from companies themselves. It was suggested in the discussion that companies should require that search firms provide a larger, more diverse slate of candidates that broadens choices and gives flexibility in recruiting talent that goes beyond the usual metrics of experience as a former CEO or chief financial officer. Companies can also consider their board tenure policy as a means to freshen a board to enhance diversity. Search firm professionals also say they can play a key role in coaching and mentoring prospective talent, especially where start-up firms are concerned. Mentoring can include training on how to create value once on a board.

What makes a good board member? By definition, board members have two main duties to the company whose board they serve on: duty of loyalty and duty of care. First and foremost, board members should act with full loyalty and utmost care, and they are bound to the highest standard, known as fiduciary duty. There is significant experience and training that board members should have as related to these responsibilities. With those duties in mind, board members are in charge of designing the company's mission and vision. In conjunction with that, a good board member should discuss every aspect of the company's strategic plan and path to execute on that plan. Critical consideration should be given to aspects of diversity, inclusion, employee engagement, and long-term sustainability of the business. Another important aspect, especially in the case of the independent directors of public companies, is the close understanding of public shareholders' views of the state of the company and its challenges, strengths, and areas of weakness. Business leaders said they look for big thinkers on strategy and a strong financial background.

## Board of Director Concerns: Critical Issues in the Energy Sector

### 1. Access to capital in light of increasingly important ESG considerations

Industries are not guaranteed access to capital. In fact, industry can have increased problems attracting top capital and moving forward to stay relevant. This is particularly relevant to many aspects of the energy industry. For example, coal mining–related companies have been removed from many investors' portfolios. As a result, the cost of capital of funding new projects has become prohibitively expensive, to the point that the coal industry is on a path of secular decline in the US and Europe. Recently, parts of the oil and gas sector are facing similar pressures. Some of the largest and most reputable institutional investors, such as sovereign wealth funds, public pensions, endowments, foundations, and other large money managers, have started relying heavily on ESG considerations, and some have gone as far as completely divesting out of traditional oil and gas companies and projects in their portfolios.

The response of energy companies has been to adopt better ESG practices in their businesses and to respond to shareholder concerns about their more transparent disclosure of ESG policies and practices.

Many of the oil and gas supermajors, especially the European ones, have now set clear goals to decarbonize their products, partially or fully, in alignment with the targets of the Paris Agreement on climate change. Workshop participants noted that this will require added diversity of thought into the workforce, into management teams, and ultimately into the boards of the energy companies. A diverse board can position a company to be significantly better equipped to monitor and challenge the status quo and find innovative and profitable paths for the companies to achieve their decarbonization goals. From a governance standpoint, board diversity also has significant positive benefits—for example, helping management avoid groupthink and reducing other biases that have been proven to lead to poorer decision-making.

Access to capital is also promoted when companies focus of improving their diversity metrics because shareholders and potential investors will increasingly consider this metric as a sign of a well-run company. As mentioned above, diversity ultimately creates better outcomes and yields better results for shareholders.

## 2. Digitization of the energy sector

The business community has reached a critical moment where industry will have to make a switch, pivoting toward digitization and automation, in all sectors. This tipping point is creating a significant change in all aspects of business. There is a thesis that this will create a huge bifurcation in the future and fortunes of energy companies: those who are willing, able, and successful in adapting to a new digitized reality, and those who will exhibit inertia and be slow to change. The former will survive, and the latter will likely underperform and potentially cease to be sufficiently competitive to survive, participants said.

Companies' ability to pivot successfully will be highly dependent on the ability to attract the right workforce, to retrain existing workforce, and to embrace change. Workshop participants noted that this has become a significant challenge for energy companies and believe their ability to attract a diverse and inclusive workforce is now paramount.

To recruit the kinds of new talent that will be needed, experts at the workshop suggested that companies' mission statements will need to resonate with the new generations, particularly younger millennials and Generation Z, who will most likely be the main agents of change in these companies' digital transformation. Business leaders presenting at the workshop provided a rich source of examples, precedents, and policies that are important in attracting the new generation of the workforce and bringing purpose, diversity, and inclusion to the work population. Emphasis on industry's culture of technology innovation, large data sets, and extreme engineering is a key tool for successful recruiting, senior leaders pointed out. But oil and gas executives and chairs of the boards noted that it is often difficult to articulate the reality that oil and gas demand is not going away overnight, and the industry can provide good jobs and sustainable products well into the future. One cultural barrier to younger workers is an orientation to want to participate in less hierarchical management teams that promote innovation and less stratification. Traditionally, the oil sector has been a top-down management structure.

The energy sector (particularly the conventional side of the sector) is facing a particularly difficult challenge attracting this workforce, given the strong fundamentals and growth expectations of the technology sector. Smart and focused policies have to be implemented to win the war on digital talent. The silver lining is that the green, sustainable, renewable segments of the energy industry (such as wind, solar, and storage) are seeing good interest from the new generation of workers. As the baby boomer generation retires from the sector, companies are now focusing heavily on recruiting millennial workers, who often have different job expectations and experiences than senior managers. Companies will have to actively articulate the data analysis and technology-heavy elements to the industry and offer more flexible work environments to compete with technology companies for new STEM graduates, consulting firms suggested at the workshop. Company leaders at the workshop said that as they work toward these new elements to recruiting and retention practices, they are having more success competing for talent.

## Conclusion

The last part of the workshop focused on perspectives from energy board members and CEOs. Leaders said they continue to find that the pool of diverse candidates, both in senior management and director positions, is very limited, suggesting more change is still needed. Speakers in this last session shared their best practices, lessons learned, and key takeaways from the diversity journeys they each have embarked upon. One company mentioned how women's attrition from the industry to go into the financial world, especially as it relates to Wall Street or private equity, is significantly lower than their male peers, pointing out a key advantage of senior women leaders. Business leaders added that they need to act fast after identifying a top candidate for board service to ensure the individual accepts the position instead of joining a competing board. Scholars also suggested that research indicates that women will show more loyalty for their employers if they are treated equally and are given the right opportunities to rise through the ranks.

# NOTES


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4. Alex Edmans, "28 Years of Stock Market Data Shows a Link Between Employee Satisfaction and Long-Term Value," *Harvard Business Review* (March 2016).

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6. National Association of Corporate Directors, *NACD Blue Ribbon Commission on Culture as a Corporate Asset*, 2017.

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