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Experience or Independence?

Director Tenure and Potential Tradeoffs: A Global Comparison

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Introduction

Director tenure has long been a subject of debate, with some fear that a long tenure may compromise a director's independence while others contend that with tenure comes experience and knowledge and that alone should not be a measure of independence. Boards and investors also often view director tenure from a board refreshment perspective, where a preponderance of long-tenured directors may signal that the board is becoming too stale.

ISS-Corporate analyzed global director tenure data and potential implications for corporate governance, highlighting the diverse approaches across different markets.

KEY TAKEAWAYS

- Long director tenure offers benefits such as institutional knowledge and stability but also raises concerns about entrenchment and resistance to change.
- Independent director tenure varies across regions, with some markets affected by regulatory limits (e.g., 6 years in South Korea and 9 in the U.K.). Other markets such as the U.S. favor longer terms, while European companies seek a more balanced approach. Most developing markets are affected by limited talent pools and evolving governance practices, resulting in shorter tenures.
- Factors beyond geography, such as complexity of the business model and ownership structures, play a crucial role regarding tenure length and should be considered when benchmarking or formulating governance policies.
- Companies demonstrating a proactive approach to board refreshment and succession planning, ensuring a healthy balance of experienced and newer directors with diverse perspectives, can benefit from global institutional investor support.

An overview of tenure perspectives

Concerns over director independence arise when a director serving on the board for an extended period develops an overly close relationship with management or becomes less attuned to shareholder feedback, potentially compromising their objectivity. This can lead to a disconnect between board decisions and investor expectations. Additionally, a lack of board refreshment can lead to lack of new perspectives and up-to-date skills necessary to navigate emerging challenges and opportunities. This risk may be particularly relevant to emerging areas such as technology, cybersecurity, and sustainability. Long tenure with limited board refreshment could inhibit the company's ability to adapt and innovate in a dynamic market and increase the likelihood of risk oversight failures.

However, there are notable benefits to longer director tenure. Experienced directors bring valuable continuity and stability to the board, leveraging their deep understanding of the company's operations, history, and network. This experience can be crucial for board leadership roles or during periods of transition or crisis, providing a steady hand and informed decision-making. Furthermore, experienced directors can serve as mentors to newer board members, reducing onboarding costs and allowing the board to focus on strategic matters.

Many jurisdictions have attempted to address these concerns through mandatory or recommended term limits with varying definitions of "long tenure." South Korea, for example, imposes a strict six-year limit, prioritizing refreshment in a market characterized by strong family influence. By contrast, the U.K. and some European and Asian markets generally favor a term limit of nine to 12 years for independent directors, balancing the benefits of long tenure with independence concerns.

REGION	MARKET	REGULATION
Europe	France	12 years
	United Kingdom	9 years ("comply or explain"-basis)
	The European Commission recommends that independent directors serve a maximum of three terms or twelve years.	
APAC	Hong Kong	9 years (starting January 2025, whilst existing companies have three years to comply).
	Malaysia	12 years
	Singapore	9 years
	South Korea	6 years

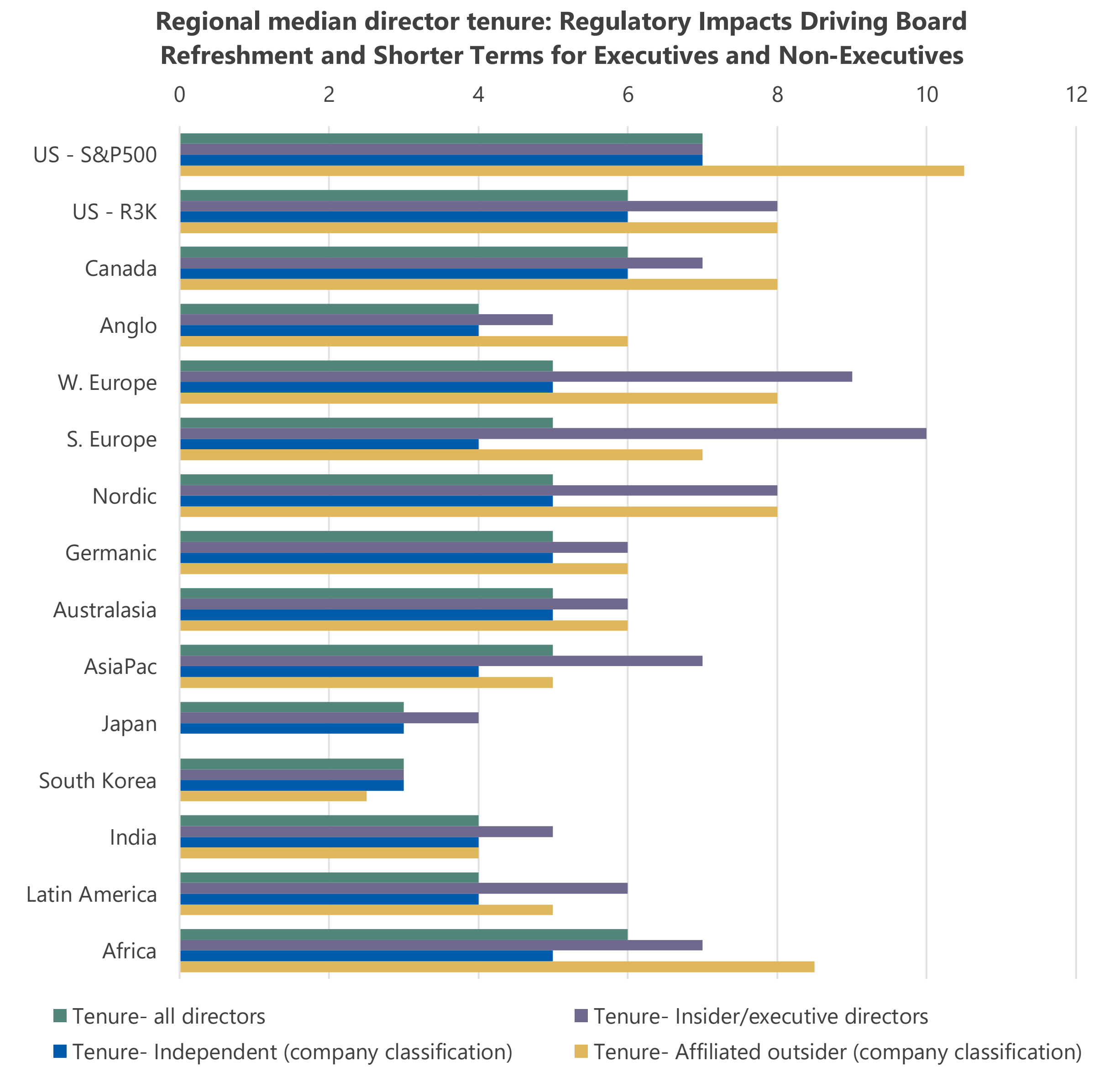
Source: ISS-Corporate

Cross-market comparison of director tenure

An analysis of global director tenure reveals stark regional differences, reflecting in part the market's regulatory and cultural norms as well as investor views. S&P 500 companies boast the longest median tenure at seven years for all director types, with little distinction between executive and non-executive directors. Europe averages five years, with executives serving between six and ten years, and non-executive directors four to five years. The U.K. represents the shortest European tenure, at five and four years, respectively.

For most Asian markets, median tenure is between three and five years, with the shortest in Japan and South Korea. Both countries have traditionally emphasized seniority in corporate hierarchies, leading to a preference for shorter tenures as a way to manage internal dynamics and distribute leadership opportunities more broadly among senior management.

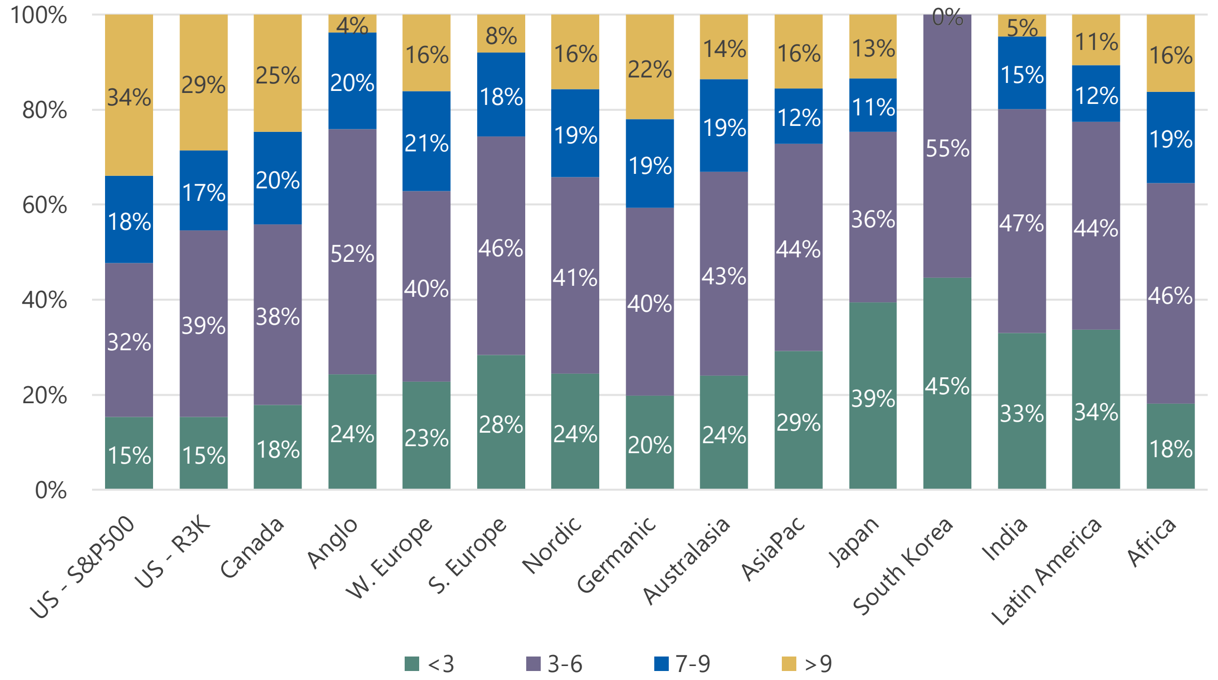
The median tenure of affiliated outside directors or non-independent non-executive directors - often possessing specialized knowledge or representing major shareholders - is similar across most regions. The exception is the S&P 500, where affiliated outsiders' tenure exceeds insiders', reaching 10.5 years. This suggests companies value their expertise, potentially accepting a trade-off between their contribution and board independence.



Source: ISS-Corporate as of January 14 2025;
Anglo=Ireland, U.K.; W. Europe=Belgium, France, Luxembourg, Netherlands; S. Europe= Italy, Spain; Germanic=Austria, Germany, Switzerland; Australasia= Australia, Newzealand; AsiaPac= China, HongKong, Singapore, Taiwan; Latin

A focus solely on independent directors reveals further regional divergence. S&P 500 companies prioritize experience, with only 15% serving under three years and 34% exceeding nine. Europe favors a more balanced approach, with half falling within the three-to-six-year range. APAC leans towards shorter tenures, with one-third serving less than three years, reflecting evolving governance practices and growing talent pools. South Korea's profile is skewed by tenure limits to notably short tenures, with almost half of the directors serving less than three years.

Independent director tenure by region: U.S. emphasizing experience, while Asian market still impacted by evolving governance.



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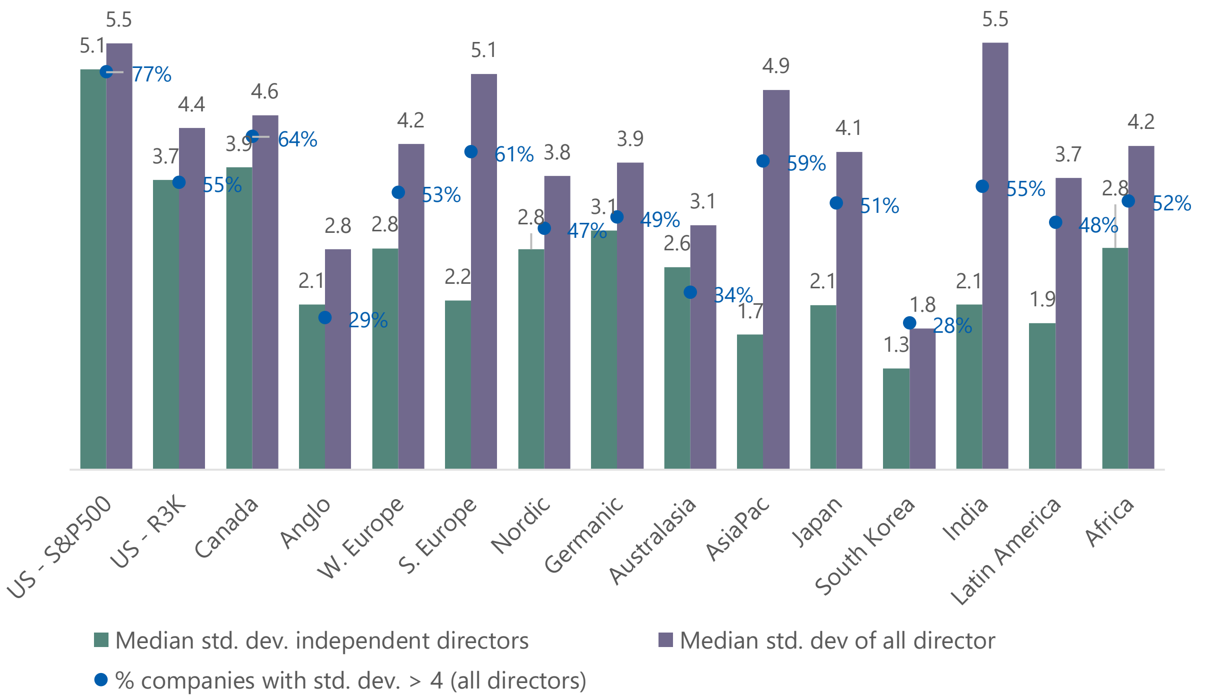
To measure tenure diversity, our analysis uses standard deviation of director tenure, measuring the spread or variation in years of service on a board within each company. A higher standard deviation indicates greater tenure diversity, with a wider range of experience levels represented. Conversely, a lower standard deviation suggests more uniform tenure and potentially less diversity of experience. The standard deviation offers a valuable starting point for assessing board tenure diversity and can flag potential issues with overly homogenous or overly volatile board compositions. Still, there are some limitations, as it does not capture nuances, such as directors' prior experience and skills before joining.

Tenure diversity also varies significantly by region. S&P 500 boards demonstrate wider experience ranges than most developed markets for entire board and outside directors, while tenure diversity is a more focal point for executive directors in Europe. The U.K. and South Korea exhibit less variation, showing that tenure limits might affect overall board tenure diversity negatively and encourage companies to focus on continuous board refreshment.

Board tenure diversity: Most markets have secured sufficient diversity across entire board, with the exception of U.K. and South Korea.

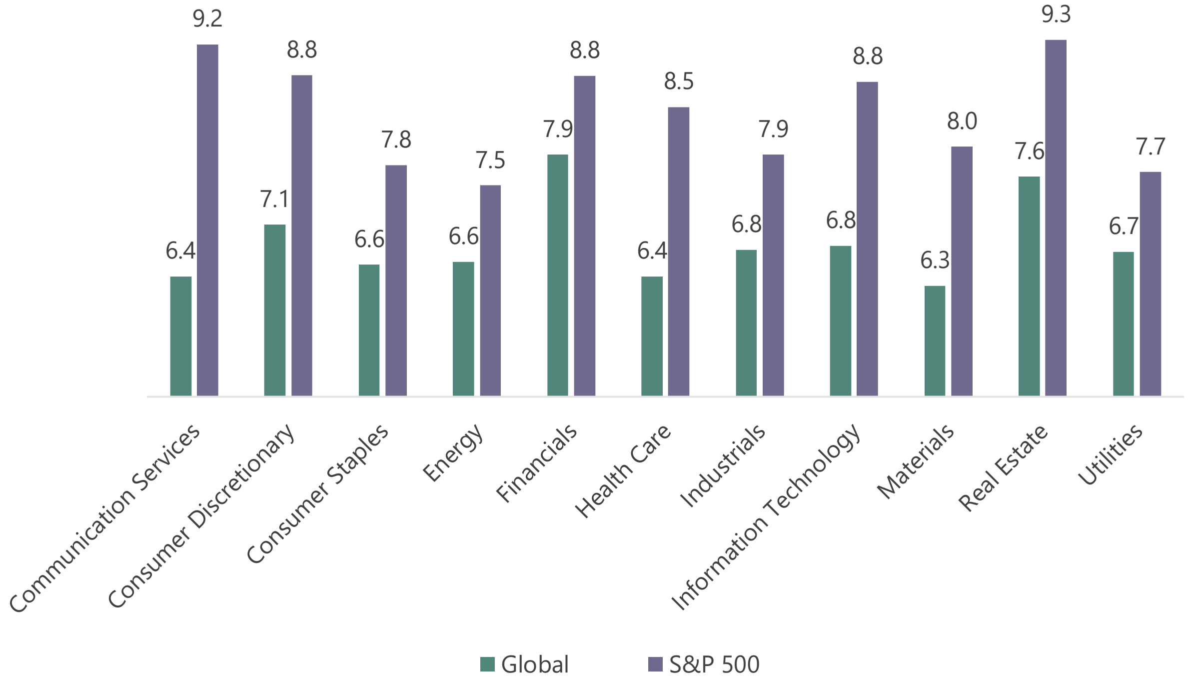


Source: ISS-Corporate as of January, 14 2025

Industry-specific expertise or complexity, ownership structure and government involvement.

ISS-Corporate found that sector plays a significant role in independent director tenure. In Financials and Real Estate, tenure often exceeds other sectors globally. In the S&P 500, this trend extends to Communication Services and Information Technology (IT). This can be attributed at least in part to complex regulations, specialized knowledge, and the need for established relationships in these industries, favoring longer tenures. Conversely, Materials and Utilities sectors have shorter-than-average tenures. A higher prevalence of founder-led or family-controlled companies in some sectors - prioritizing continuity and long-term vision - could translate into longer tenures for trusted directors. The presence of a dual-class shareholder structure may also slow the adoption of governance best practices like board evaluations and term limits.

Average independent director tenure length: Financials and Real Estate sector more likely to have independent directors with lengthy tenures.



Source: ISS-Corporate as of January, 14 2025

Key Action Points: Balance independence requirements with the need for institutional knowledge and experience, while maintaining a transparent approach.

For corporate issuers, effective board tenure management is crucial, and a proactive approach ensures optimal board composition, promoting long-term shareholder value:

- Regularly review board composition, balancing skills, tenure, and background.
- Strive for a mix of tenure lengths, balancing experience with fresh perspectives for both inside and outside directors. Succession planning should explicitly address this balance.
- Engage with shareholders to understand their perspectives on board tenure and diversity, crucial for sound governance practices.

- Justify the value of long-tenured directors, especially those nearing 10 years, to anticipate investor scrutiny
- Maintain a robust pipeline of potential candidates and conduct scenario planning to address potential activist challenges or unexpected departures.
- Regularly evaluate individual and overall board performance, assessing individual director contributions, considering both experience and potential complacency related to tenure and board dynamics.
- Companies lacking transparent approaches regarding the benefits and risks of long tenure may face lower support rates for nomination committee chairs or vulnerability to activist campaigns.

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