GREAT MINDS DON'T THINK ALIKE
COGNITIVE DIVERSITY IN THE BOARDROOM
As part of a leading UK-based financial services group, we’re committed to ensuring an inclusive environment for our customers, colleagues and communities. Getting this right is at the heart of our purpose of Helping Britain Prosper.

In 2014, as a Group, we became the first FTSE 100 organisation to make a public commitment on gender equality and in 2018 we were pioneers once again, becoming the first FTSE 100 firm to set an ethnic diversity target. In 2020, we launched our Race Action Plan further articulating our public commitments on steps we are taking to make our culture and our business more diverse and inclusive.

Today, our commitment remains. We aspire to be even more reflective of society with pledges to increase representation of our senior leaders by 2025 to 50% for females and 13% for Black, Asian and Minority Ethnic colleagues.

And now diversity of thought (also termed cognitive diversity) finds itself as a topic more important than ever on the diversity agenda. A recent report from the FCA recognises diversity of thought as a fundamental factor required to tackle the complex and evolving issues across the financial sector and wider society.

For me, as a Spaniard working in a British organisation, I always wondered whether my culture and my upbringing would affect the way in which I would be able to integrate myself into a company with such a long heritage and effectively lead our colleagues with empathy. However, whilst it does mean that I may not always catch on to the British sarcasm, it does not hinder the conversation with my team and the decisions we make. Instead, it allows for a more nuanced approach to our thinking through the sharing of experiences from distinct cultures and countries.
Ultimately, my team and I share a sense of responsibility on setting the direction for the future and this benefits hugely from having an array of perspectives and diverse views being brought to the table.

But cultural identity is only part of the overall picture. Other indicators, such as age, gender identity, race, sexual orientation, religion and disability (to name a few) also have a part to play in the way we think. And this is why I’m proud that Scottish Widows is recognising cognitive diversity in the boardroom as one of our core priorities.

As one of the UK’s biggest pension providers, we have a duty to deliver the best possible retirement outcomes for our customers. And this includes working with our investee companies to achieve better corporate governance through board diversity – making sure this includes a focus on diversity of thought, in addition to addressing some of the more obvious inequalities in the room such as under-representation of women and ethnic minority groups.

In doing so, investment and other decisions will be better thought through, with all angles considered. We should not shy away from a culture of constructive disagreement – rather, we should encourage such an environment for leaders and decision makers to thrive.

This is a relatively new concept to many of us and we know we won’t always get things right; however, the important thing is that we’re open to learning, embracing difference and encouraging other companies to do the same. After all, a diverse business is a better business.

ANTONIO LORENZO
Chief Executive
Scottish Widows and Group Director, Insurance and Wealth
INTRODUCTION

Board diversity has improved over the last decade, particularly with regards to gender. This has resulted in greater representation and use of the diverse sets of skills and expertise across corporate leadership in the UK economy. It has also resulted in British business being able to claim parity of diversity with many of its European and global business partners.

However, while the inclusion of more women on company boards has forced the candidate pool for board positions to expand, it has not fundamentally changed the nature of the pool. Elite school, previous ‘city’ experience, qualifications such as chartered accountancy or law degrees, and previous CEO experience are still seen as important signals of competence to recruiters and board chairpersons alike. Racial diversity on boards has also failed to improve in-line with the Parker Review recommendations.

To build boards with the strength to meet the enormous challenges we face, true breadth of knowledge, experience, and expertise is required. That’s why cognitive diversity – bringing together a range of different styles of thinking – is so important.

Cognitive diversity is becoming more widely written about. Seminal works like Matthew Syed’s 2019 book, Rebel Ideas, are now seen as increasingly influential in management and leadership circles. It even found its way into the public’s consciousness during the men’s 2020 UEFA European Football Championships through England manager Gareth Southgate’s approach to listening and learning about a broad range of sports to influence his tactics and player management.

But while there may be increasing attention given to cognitive diversity, very little has been written about making a business case for it. This report attempts to address this omission and deliver usable information to a broad range of stakeholders through bringing together existing research. The report aims to provide commentary on the subject, based on academic research and interviews, in an accessible format.

1 Ethnic diversity of UK boards: the Parker review – GOV.UK (www.gov.uk)
Scottish Widows is a significant shareholder in many of the world’s companies. We hold shares on behalf of customers who invest with us. As a result, we are the stewards of these investments and have a responsibility to manage and protect them in the best way possible.

We believe cognitive diversity in leadership – including individuals who have different styles of problem-solving and can offer unique perspectives because they think differently – leads to better long-term value creation for the companies we invest in and, hence, our customers. This report aims to define cognitive diversity and provide guidance for the companies we invest in.

The findings of this report are based on academic articles and papers on the subject, including those focused on executive teams, supported by interviews used to test ideas and inform understanding. We found directors were aligned with the findings from the literature, and the key themes emerged in both the studies and interviews.

We reviewed 17 academic journals and interviewed seven directors, two board chairs and one board recruiter. We are very grateful for everyone’s contribution and their willingness to speak openly about this emerging topic.

The information we got from directors, in particular, played a significant role in our research. We asked them for their personal views and experience of cognitive diversity on boards to give us practical insight.

The majority of directors we spoke to were European with one from Asia and one from Africa. In countries with less developed corporate governance, cognitive diversity wasn’t necessarily missing, but boards were more likely to face issues around independence, which affected the success of the cognitive diversity. Board members’ paths to success could also be more difficult in these countries.

The report was written by the Responsible Investment Team at Scottish Widows in collaboration with Dr Johanne Grosvold, Associate Professor of Corporate Governance and CSR, School of Management, University of Bath.

Dr Johanne Grosvold is an associate professor of corporate governance and corporate social responsibility at the School of Management, University of Bath. She is the Deputy Director for the Centre for Business Organisations and Society (CBOS), the largest research centre in the School of Management. Her research sits at the intersection of corporate governance and social and environmental management. She has a particular focus and interest in corporate boards and has worked in the field for over 15 years. Prior to her academic career she worked in investment banking and investor relations.

More details about the methodology can be found in the appendix.
WHAT IS COGNITIVE DIVERSITY?

In 1998, Miller, Burke, and Glick defined cognitive diversity as a ‘variation in beliefs concerning cause-effect relationships and variation in preferences concerning various goals for the organisation’. However, Van Knippenberg, Ginkel, and Barkema (2012) it was more about perspectives and understanding team members’ points of view. They suggest creativity is realised through cognitive diversity when team members actively engage in what they term ‘perspective taking’ (putting yourself in the position of your team colleague), with a view to facilitate information elaboration.

Reynolds and Lewis (2017) state that cognitive diversity is not predicted by factors such as gender, ethnicity, and age. Instead, they define it as ‘differences in perspective or information processing styles’. The relationship between cognitive diversity and demographic factors, such as age, is one area this report seeks to better understand.

Lastly, Martins and Sohn (2021) discuss cognitive resources rather than cognitive diversity. Cognitive resources are the skills, insights, knowledge, and abilities team members can employ for the good of the team. The more plentiful and diverse the cognitive resources available to a team are, the better the team is at solving complex challenges.

For consistency, we’ve chosen to use the definition of cognitive diversity used by the Prudential Regulation Authority (PRA), the Financial Conduct Authority (FCA), and the Bank of England (BoE) in their recent discussion paper (DP), Diversity and inclusion in the financial sector – working together to drive change, which is:

‘Bringing together a range of different styles of thinking among members of a group. Factors that could lead to diverse thinking could include, but not limited, to different perspectives, abilities, knowledge, attitudes, information styles, and demographic characteristics, or any combination of these’.
Strictly speaking, we are all cognitively distinct as we all have individual experiences and attributes. People are not defined by one diversity trait, but by a combination of factors that lead to different perspectives that change over time as we grow and have more experiences.

**REPRESENTATION**

Cognitive diversity has grown out of the more established concept of ‘representation’. It is now well established in business and government that our institutions should make every effort to represent society. Having got to this point, we can now think deeper and broader about what being representative should mean.

Catherine Seierstad discusses social justice in her research on female board directors who had all benefited from the quota for women introduced in Norway in 2005.\(^5\) The research states women and men should have the same access to seats of power based on the inherent notion of broadly equal distribution of skills and experiences. In addition, it is evidently unfair if power and resource is concentrated, and the social justice argument essentially argues for redistribution of power.

Representation from across society has multiple benefits, which include inspiring future generations, designing products and services to suit the needs of everyone, as well as making sure some groups are not left behind. There is no doubt that representation of a broader spectrum of society adds value to the workplace. Cognitive diversity is an additional layer to reach more people and contemplate how different approaches can contribute to the discussion.

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One interviewee said there was some confusion around the term.

“I think most people understand the importance of avoiding groupthink, but when it comes to how you define and identify cognitive diversity, there is some confusion.”

- Board recruiter
As firms face increasingly fast moving and ultra-competitive environments, executives and boards are required to respond quickly to uncertain, volatile conditions. Executives must be able to identify opportunities and threats, and respond with strategic solutions in tight time frames. The wide range of risks and opportunities require executives with different experiences and perspectives and, therefore, diverse cognitive capabilities.

Company boards tend to be elite by nature, experts in their field, and non-executive directors are often CEOs of other companies. However, boards of directors differ from other professional teams in that while they are responsible for sanctioning corporate plans, they are not directly responsible for implementing them. Consequently, the board’s output is entirely cognitive or thought-based.¹

That means understanding what cognitive diversity is, and how to harness it effectively, is particularly important.

**FINANCIAL VALUE CREATION**

As cognitive diversity is difficult to quantify and therefore measure, it is not possible to assign figures to the impact of cognitive diversity. Issues around causality and data quality mean proxies, such as gender, are used to establish relationships between diversity and performance. McKinsey has been examining diversity for several years, and their 2015 *Diversity Matters*² report found:

- Companies in the top quartile for racial and ethnic diversity are 35% more likely to have financial returns above their respective national industry medians.
- Companies in the top quartile for gender diversity are 15% more likely to have financial returns above their respective national industry medians.

McKinsey argues that diverse companies perform better for a variety of reasons, including winning top talent, improving customer orientation, and employee satisfaction. They go on to say this suggests other types of diversity, including experience and mind-set, are also likely to bring some level of competitive advantage.

There is a range of studies covering the positive relationship between diversity and performance which suggests that cognitive diversity would also have a positive correlation with performance.

- A 2019 International Finance Corporation study found portfolio companies in emerging markets with gender-balanced leadership teams outperformed in valuation increases by as much as 25%, compared with non-diverse teams.³
- The Refinitiv D&I study:⁴ Key factors driving diverse and inclusive workplaces, found there was outperformance in a number of portfolios that took diversity of employees or boards into account.
- The most gender-diverse companies globally outperformed their regional benchmarks by 1.7%.⁵
- Firms with female CFOs are more profitable and generated excess profits of $1.8trn, 2002-2019.⁶
- Top quartile companies for ethnic/cultural diversity at exec level were more likely to have industry leading profitability by 33%.⁷

“Not thinking about cognitive diversity is a risk. I have seen the impact of groupthink in the past.”

Chairperson, male, financial services.
However, the purpose of increasing cognitive diversity is not purely to increase profits. The benefits of cognitive diversity are also associated with managing risks, seeking opportunity, and equipping businesses for an uncertain future.

**COGNITIVE DIVERSITY BENEFITS**

The positive impact of cognitive diversity cannot be overstated for well-functioning teams. Research shows it can bring all sorts of benefits to corporate boards, from problem solving and decision making to building trust. Cognitively balanced teams take less time to solve problems. Teams who can consolidate their knowledge and are willing to learn new things were found to resolve problems quicker. A range of educational backgrounds and experience were found to be key contributing factors. But their potential can only be realised fully with the right leadership – on their own, the benefits of these characteristics cannot be guaranteed. They need the right guidance to fully develop.

It is also important to consider social cognitive diversity when thinking about performance-based benefits. The ability to understand other people’s viewpoints and where they are coming from in their thinking can help foster trust in a team. Social cognitive capability can also be useful for managing resistance to change and stopping company boards standing still.

Confidence bias also plays a part. Apfelbaum and Mangelsdorf found that mistakes and inaccuracies happen more frequently in homogenous groups, as people are more likely to copy each other’s mistakes. This is known as confidence bias. Diverse groups are more likely to avoid confidence bias as fewer people are willing to go along with a bad decision.

An executive team’s cognitive, emotional, and behavioural potential does not only shape employees’ professional experiences, it also impacts the strategic decisions executive teams make. Raes, Bruch, and De Jong (2013) state: ‘Leaders can influence productive energy, because they shape employees’ emotional experiences, their cognitive interpretations of organisational events, and their productive behaviours, through which energy is generated.’ In their study, 5,000 team members and 200 executives surveyed agreed that the more cohesive and better integrated the executive team was, the more cognitive capacity employees had to expand on their work.

In other words, if executive teams are working well, the teams under them are also more likely to be working efficiently and proactively.

All the directors we spoke to agreed cognitive diversity was a key factor in the success of board decision making. One even thought it was a good way to engage people on diversity in general, as it was more easily understood as being relevant to decision making than arguments about representation.

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To answer this question, we took a look at the companies which make up our biggest investments. They are all large companies located around the world. Using publicly available information from each of our top 25 holdings, we found only one firm which specifically mentions ‘cognitive diversity’ as something they consider in their working practices.

However, cognitive diversity can be more widely defined as diversity of thought, which is a concept mentioned with more frequency. Of the 25 firms, 10 mention this as an area they consider as part of their wider diversity initiatives.

Encouragingly, there’s no shortage of diversity initiatives relating to demographic diversity. 22 of the 25 firms, for example, have multiple dedicated initiatives for gender, race and ethnicity, disabilities, and LGBTQ+ in place.

18 of the 25 firms have been recognised for their diversity practices. Several feature in prominent diversity recognition schemes, such as ‘Forbes Best Employers for Diversity’, ‘Stonewall Employers’, and ‘The Times Top 50 Employers for Women’.

The vast majority of our top holdings are keeping up with large scale events that put diversity practices under the microscope. 20 of the 25 firms made fresh commitments to their anti-racism/black community initiatives. These commitments range from more robust financial backing to implementing race action plans with new targets for inclusion of black colleagues.

It appears cognitive diversity is a topic companies are aware of, but have yet to take structured action at board level or otherwise.
Diversity considerations are increasingly becoming a regulatory requirement for companies. The joint Discussion Paper, 21/2, issued in July 2021 by the PRA, the BoE, and the FCA titled: Diversity and inclusion in the financial sector – working together to drive change, aims to ‘accelerate the pace of meaningful change on diversity and inclusion’ in the financial sector. The paper explicitly defines diversity to include cognitive diversity. The paper also sets out the importance of data collection to understand diversity and track change. The paper makes for the following case for diversity:

‘Diversity makes business sense – from both a financial and a consumer perspective. It can lead to better outcomes for firms, support their safety and soundness, and promote financial stability. We believe that more diverse and truly inclusive firms will benefit from better risk management, as individuals will feel more empowered to have open discussions and debates, without fear of having their views shut down.’

**Discussion Paper 21/2: Diversity and inclusion in the financial sector – working together to drive change**

Ahead of the consultation on diversity and inclusion in the financial sector, the FCA conducted a literature review, which provides evidence of the impact of diversity and inclusion in the workplace.

**Literature review findings:**
- Gender diverse senior leadership is associated with positive business performance outcomes, especially when there is a ‘critical mass’ of women (three or more).
- Gender diverse senior leadership appears to lead to positive risk management outcomes.
- The evidence for the impact of gender diverse boards on regulatory conduct outcomes – including corporate governance monitoring, meeting frequency, and the quality of information disclosure, as well as evidence of fraud and misconduct – all points to women’s positive influence.
- Diverse teams can have differences of opinion, but are more innovative and better at solving problems creatively.

In July 2021, the FCA also published a consultation paper: Consultation Paper 21/24: Diversity and Inclusion on company boards and executive committees. The paper proposes changing company listing rules:

‘to require companies to disclose annually on a comply or explain basis whether they meet specific board diversity targets and to publish diversity data on their boards and executive management.’

The direction of travel is clear – compiling diversity data will become mandatory for companies, so not treating the subject seriously will soon become a regulatory risk. Improvements in diversity data will contribute to environmental, social, and governance (ESG) data accuracy overall and potentially filter through to investment decisions.

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8 FCA, 2021. Online here: DP 21/2: Diversity and inclusion in the financial sector – working together to drive change | FCA
9 FCA, 2021. Online here: DP 21/2: Diversity and inclusion in the financial sector – working together to drive change | FCA
The relationship between demographic diversity and cognitive diversity was a key area of interest in the research. It is worth stating that demographic diversity in its own right should be pursued because of the importance of businesses and government representing the communities they serve. Our findings have shown demographic diversity contributes to, but does not guarantee, cognitive diversity.

Some progress has been made in the UK, but there is still room for significant improvement.

The Parker Review\textsuperscript{10} considers how to improve the ethnic and cultural diversity of UK boards. The 2020 review reports that targets for representation of people of colour on boards haven’t been met.

- There are 172 directors of colour in the FTSE 350.
- This is only 7.5\% of the total number of directors.
- In the FTSE 100, 31 out of 83 companies, and 119 out of 173 companies from the FTSE 250 which provided data, had no people of colour on their boards.

The Hampton-Alexander Review\textsuperscript{11} focuses on increased female representation on FTSE boards and women in senior executive positions.

The latest report (2020) suggested the targets set by the review have largely been met:

- 36.2\% of FTSE 100 boards are women.
- 33.2\% of FTSE 250 boards are women.
- 34.3\% of FTSE 550 boards are women.
- 30.6\% of FTSE 100 executive committee and direct reports are women.

\textsuperscript{10} Ethnic diversity of UK boards: the Parker review – GOV.UK (www.gov.uk)

\textsuperscript{11} FTSE women leaders: Hampton-Alexander review – GOV.UK (www.gov.uk)
GENDER

Research has shown that attributes of a woman’s gender have a specific contribution to make. One example of this is through their supposed emotional intelligence. This isn’t to say all women make this contribution and that men cannot also contribute this way, but it is a recognised factor which can contribute to the overall cognitive diversity of the board.¹⁰

Talents and skills are roughly equally distributed between genders.¹² Systematically limiting recruitment to only the male half of the talent pool means you do not optimise the team.¹⁴ In her research of women on boards in Norway, Seierstand found that women were often not ‘seen’ before the quota, as they were outside of male networks even if they had better formal qualifications and experience.¹⁵

A chairperson we spoke to felt gender had a significant impact on board dynamics.

Female directors who have only recently been recruited to a board position may find it difficult to appreciate the impact of their recruitment. The majority of boards have made good progress recruiting women, and it may be the case that better gender representation has become the norm and, therefore, the impact of gender is not as present in directors’ minds. Moving forward, as boards work to increase other aspects of diversity, it is important to remember the difference women have already made to the board environment.

Several female directors felt their nationality and socio-demography was more of a differentiating factor than their gender. There was also acknowledgement that a couple of women on a board could not represent the female population as whole, which is true of all demographic factors.

“I believe there are women who are ready for board appointments. It’s just finding them.”
Non-executive director, female, financial services.

“My upbringing in the North East of the UK has shaped the diversity of my thinking.”
Non-executive director, female, financial services.
ETHNICITY
A 2019 study demonstrates the performance-based benefits of ethnic cognitive diversity. Smulowitz, Becerra, and Mayo analysed ethnically diverse lawyers in a predominantly white profession, and the potential benefits their differing backgrounds, educational experiences, and perspective could bring. The study found increased ethnic diversity could lead to financial benefits.

A key component of diversity is inclusion. People need to feel comfortable bringing their true selves to work and to feel like they are in a safe psychological environment.

Notably, the Smulowitz, Becerra, and Mayo study found that lawyers were often promoted when they held a certain type of ‘cultural capital’, such as preferred hobbies, a certain way of dressing, and holiday destinations. Ethnic minorities were only promoted if they shared these cultural references. Aside from the obvious issue of equality, this type of hiring can potentially override cognitive diversity benefits.

OCCUPATION
As well as socio-demography, occupation was a recurring theme which directors felt influenced cognitive diversity. Many felt the training and experience of accountants, for example, led to individuals who were concerned with liability and risk, while those with marketing backgrounds tended to approach problems more creatively.

Directors felt it was important to ensure their boards were comprised of people from different occupational backgrounds to safeguard against people in the same profession with similar traits dominating. Rather than gaining insight from other professions, a lack of balance could lead to everyone on a board reacting in the same way to problems. Two board members spoke about the need for people in specific occupations to be represented on boards going forward, such as ecommerce, acknowledging that changes in business required new skills.

AGE
For younger board members we spoke to, their age was an important factor as it contributed to them following different paths and having different experiences to the generations before them. This led to them having an alternative outlook on life and may have also resulted in them entering more ‘modern’ careers, such as ecommerce. This experience could bring something different and contribute new ways of thinking.
DIRECTORS’ VIEWPOINT

We were particularly interested to hear what the directors we interviewed had to say about demographic diversity. They cited nationality, ethnicity, and regional upbringing as the most common indicators of cognitive diversity. One felt living in different communities was a key influence as it enabled them to appreciate different cultural contexts. The intersectionality (the interconnected nature of social categorisations such as race, class, and gender) of someone’s personality traits was also raised as a framework to be considered in diverse hiring.

Lifestyle factors are also a consideration. Many board members have a certain type of lifestyle, which can make it harder to understand the issues facing future directors, such as childcare costs, caring responsibilities, or other family obligations. Only a small percentage of people can afford a nanny, for example.

Customer understanding also came up as a key skill. A board cannot fully mirror the population, so members need to be willing to listen to and understand their customers and stakeholders.

We found different characteristics which are used as proxies can impact cognitive diversity in different ways, but there are not hard and fast rules. The key thing is to recruit with difference in mind and be open to how different characteristics can change the board dynamic for the better.


"People aren’t always their stereotypes – people from the same background can have very different views of the world. It is all about looking for difference – listening to the questions people ask, and how, and not just the answers they give. You can gather clues from people’s characteristics, but listening is more important."

Chairperson, male, financial services.
HOW TO MAKE COGNITIVE DIVERSITY WORK

A STRONG CHAIRPERSON IS ESSENTIAL

“The chair pushed other directors to answer my question properly – had my back from the start.”
Non-executive director, female, financial services.

“Structure of the agenda is important – gives space for important topics to focus on what really matters.”
Chairperson, male, retail.

The role of the chairperson as a facilitator was described by directors as vital to the success of diversity on boards. The ability to promote robust discussion and make people feel comfortable was crucial, especially when navigating comments or challenges that could be perceived as personal.

“Role of the chair is very important. As soon as the discussion becomes destructive you have a real problem. The role of chair is to make people understand each other’s view.”
Chairperson, male, financial services.

The role of the chairperson was especially important to new directors and non-executives. Being new requires a learning process to fully understand what is involved in any role. Directors spoke about finding their voice and how having a supportive chairperson is helpful in facilitating this. It can remind them that their difference is valued and give them the confidence to constructively challenge topics where appropriate.

One director said given the choice between a new board member with a skill set the board needed and a chairperson who can facilitate properly, the chairperson was more important.

CRITICAL MASS

This is the theory that a certain number of people with a shared diversity trait are needed for their voice to be heard. If there are enough in the sub-group to form a critical mass, both groups are more likely to be viewed as equal. The theory of critical mass demonstrates that it is important to target a broad range of diversity traits and not attempt to tick boxes.

An example of this is women on boards. Research has shown at least three are needed on a board for their voice to be considered the norm and not just the ‘voice of the woman’.
BUILDING CONNECTIONS AND TRUST

While chairs obviously have a key role in making board members feel comfortable, members can play their part too by working on their individual relationships. This influences the quality of decision making. Members with goods relationships will trust each other, so difficult conversations and challenges will be easier to deal with when they arise.

An effective board needs a shared purpose for the members to work as a team. A board functions best if it is given space to build rapport, discuss strategy, and test ideas outside the confines of the board room and formal meetings.

One director told us they believe values are essential to success. All board members need to have a shared vision for the company and understand its culture and ways of working to succeed. If a company is in need of a change of direction, multiple viewpoints can help support the necessary decision making. Cognitive diversity adds most value when board members understand the collective challenge and their unique contribution.

“Reflecting the culture of the business in board meetings is important, but more so is to get out into the business itself, to get a real sense of the values being lived as part of that culture.”

Chairperson, male, retail.

KNOWLEDGE REQUIREMENTS

Requirements for a board appointment are usually very specific – board members normally need to have a good baseline business knowledge, as well as some specialist expertise. This can potentially be a barrier for individuals who have had careers outside of the corporate world, for example. The pandemic has also worsened career development for many people.

The 2020 Scottish Widows’ Women and Retirement Report found the pandemic has polarised the UK population. Many people have lost their job or had their income reduced. As well as suffering more with job losses, those who have remained in employment are more likely to have taken on significantly more caring responsibilities during the pandemic.

This combination of economic hardship, and unpaid care and domestic work, results in difficulties for progression and career development, which then impacts diversity in workplaces and talent pipeline development for senior positions. This issue is regularly cited, and the pandemic has made it even harder.

This impact of the pandemic was also present in directors’ minds.

“I feel very concerned about the impact of the pandemic on the pipeline. It has already reduced the number of female directors.”

Non-executive director, female, retail.

Setting up a separate non-official board – or shadow board – made up of people from different career backgrounds can bring a fresh perspective and outlook to a business, as can a youth board with members too young to generally be considered as board members.
TENURE

The tenure of board members is also a factor, especially when linked to effectiveness and diversity. Boards have changed over the years and now have much broader remits, which includes topics such as sustainability. Shorter terms for directors could be one way to increase specific expertise for set periods of time.

COMMUNICATION

Just about every director interviewed said it was really important for board members to communicate well with each other. It was noted it is easier for people who are similar to understand each other as they can speak in a shared language or ‘shorthand’.

There was also an acknowledgment among directors that having people with different perspectives represents a challenge because of the time and skills required to understand each other. The majority of the directors we spoke to commented on using personality type tests to help understand how each person communicates and processes information. This practice was felt to be more commonplace at executive rather than board level, however.

“I’ve seen situations where some board members have assumed other directors are forming a clique, because they always seem to be aligned in their views, but when they did some analysis of their individual and team cognitive preferences, they understood that those directors just seemed closely aligned because they shared a very similar working style.”

Board recruiter.

Splits among board members can occasionally happen, where one group becomes dominant over another, or is at least perceived to be. This makes communication essential, as understanding how people work contributes to improving working relationships.

“Shorter, more dynamic board terms might provide, in some cases, specialist knowledge when it’s really needed for the time it’s needed.”

Chairperson, male, retail.

“When people are similar, they can speak in shorthand and it’s quicker to make a point. When people are more diverse the challenge is having the time and skills to ensure people understand each other.”

Non-executive director, female, financial services.
TEAM DYNAMICS

When new directors are appointed, it can take time for them to make their mark. This can be particularly true for directors from ethnic minorities. Progression to positions such as chairperson or a member of a key committee can be harder to attain. Inclusion of people from different ethnic minorities in key positions needs to become the norm rather than the exception.

Zhu, Shen, and Hillman looked into the concept of perception in 2014. They found age, degree-level education, university attended, and functional and industry background can all help a minority director’s position be re-categorised by others.

On the other hand, when directors have significantly different characteristics, strategic dissent, or ‘divergence in ideas, preferences, and beliefs’, can lead to executives not being willing to discuss anything that differs from their own beliefs, especially if these beliefs have been in place for a long time. This can lead to a lack of knowledge-sharing.

This is key to thinking about cognitive diversity. It is human nature to find connections and similarities with people, but shared characteristics generally mean a shared cognitive approach too. The board might feel comfortable if there is a lot of agreement, but that doesn’t necessarily mean the right decisions are being made. Differences can cause tension and have to be managed well to yield good results.
RECRUITING FOR COGNITIVE DIVERSITY IN THE BOARDROOM

RECOMMENDATIONS

BEFORE HIRING
Revisit recruitment criteria
Board criteria has lengthened significantly over recent years and it is worth revisiting which skills are essential. Rigid criteria can restrict broader representation and reduce cognitive diversity.

Widen the pool of candidates
It is worth considering candidates that might not meet all criteria, but have experience or a specific skill which is lacking from the board. For example, a CEO from a non-governmental organisation (NGO) might normally be overlooked, but they could bring vital experience and a new dimension. By identifying an individual that could cause collective challenge there is the potential to identify blind spots.

DURING HIRING
Engage with recruitment agencies
Recruitment agencies have shown their ability to increase diversity on boards and are crucial stakeholders to engage on cognitive diversity when hiring. However, agencies can sometimes be guilty of following a familiar path, so if a board is looking for something different, it is important to spell it out at the outset and work collaboratively.

ONCE HIRED
Board induction
Board members need to feel confident and comfortable in the board room to be able to ask the questions that matter. Quality inductions and support outside the board room allow time to focus on discussion and strategy during the meeting.

AFTER HIRING
Board reviews
The best way to understand cognitive diversity on the board is to test it. Personality and working style tests are a good place to start, as well as honest discussion about how well the board is functioning. Set aside time on the agenda to discuss how the board feels it addresses current and future challenges, and be open to acknowledging collective cognitive blind spots.
There is certainly room for improvement in terms of trustee board diversity in the pension industry, as trustees face similar challenges to directors. We recognise we are a part of that industry and it’s up to all of us to work on getting our own house in order.

The good news is that the pension industry is starting to take the issue of cognitive diversity seriously. The Pension and Lifetime Savings Association (PLSA) has set up a diversity and inclusion toolkit,15 for example, and The Pension Regulator now has a committee in place to tackle the problem, which will lead an internal and external diversity and inclusion agenda. Corporate Adviser has also published a report to show the pension industry why diversity is important and how to improve it.17

Influential not-for-profit initiative NextGen – Pensions, which was set up in 2018 to increase cognitive diversity in the pension industry, is at the forefront of change. They released their report, Recruiting for a cognitively diverse workforce report in May 2021.16 The report acknowledges under-representation and suggests ways the pension industry can improve their recruitment practices and attract more people to the industry.

The previously mentioned PRA, FCA, and BoE joint Discussion Paper discusses the specific role of financial markets in society:

‘Having firms that represent the society they serve would support the design of financial services and products that improve consumer outcomes. An inclusive culture in which all staff can speak up allows the benefits of diversity to flourish. Together, diversity and inclusion can reduce groupthink, encourage debate and innovation, and thereby improve outcomes for consumers and across markets, supporting financial stability.’

15 PLSA Diversity & Inclusion Made Simple Guide March 2020
16 NextGen – Pensions Recruiting for a cognitively diverse workforce research and insights 2021
17 Corporate Adviser Intelligence. Guide to Diversity and Inclusion in DC Pensions. (2021)
A CHAIRPERSON’S GUIDE TO IMPROVING COGNITIVE DIVERSITY

1. HOLD REGULAR ONE-TO-ONES

One-to-one meetings can help the chairperson develop a deeper understanding of individual directors’ views, opinions, experience, and how they can inform board discussion. It also provides a safe space to air less commonly held opinions, delve deeper into topics, and allow trust to develop. Giving individuals time to discuss issues and put forward their ideas without the other board members’ influence is a valuable and powerful way of finding out how others think, as well as what motivates and inspires them.

2. PLAY DEVIL’S ADVOCATE

Looking at something from an opposing point of view encourages healthier debate. Ideas can benefit from new perspectives, improvements can be made, and what starts off as an embryonic idea can better develop into a well thought through, coherent course of action for the company.

3. BE AWARE OF YOUR OWN PERSONALITY

An effective chairperson needs to be aware of their own biases and prejudices and have a thorough understanding of their individual strengths and weaknesses. Knowing whether they are somebody who sees opportunities and takes risks, or is more analytical and cautious, can help them appreciate how their views might differ from others, and how differences within the board can be put to good use.

4. REVIEW RECRUITMENT CRITERIA

This is vital when thinking about cognitive diversity. Board recruitment is usually constrained by pre-set standard requirements. Certain ‘must-haves’, like accounting credentials or risk management expertise, are in place to safeguard shareholders’ interests. But other considerations, such as city experience or elite university credentials, can often hinder identifying a wider range of candidates, which can mean less cognitive diversity.
5. EMBRACE DIFFERENCE
If a new director with different experiences to the existing directors is appointed, a chairperson might instinctively want to look for common ground to develop rapport and trust. This can ease the working relationship, but the chairperson should use the trust built up as a baseline for constructive debate rather than focusing on what both parties hold in common.

6. REVIEW THE BOARD REGULARLY
Board reviews can be an effective way for the chairperson and the board to reflect and assess their team dynamics, performance, and composition. Objective input is important, so a board consultant, shadow board, or similar can be useful to provide an outside perspective on performance.

7. FOSTER STRONG TEAM CULTURE
It is vital the board feels and acts like a cohesive team, even if some directors, especially non-executive directors who do not work for the company, might see themselves as outsiders or a minority. The chairperson has a central role to play in fostering a strong team culture, team trust, and in setting the tone for the work of the board. This is especially important to help the board harness its cognitive diversity.

8. BE COMFORTABLE WITH CONSTRUCTIVE TENSION
Diversity of views can be hard, messy, and uncomfortable. It is up to the chairperson to create an environment where being ‘comfortable with the uncomfortable’ is encouraged. This approach enables board members to freely challenge topics and openly debate issues. When meetings are infrequent and short, but the agendas are long, creating the appropriate environment can be difficult. However, setting aside time to explicitly ask what board members disagree with, where they believe problems lie, and what they see as the board’s blind spots in decision making, can encourage debate and create a culture that can benefit from diversity.

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Today’s boards need to respond to uncertain, fast-paced, volatile environments, and identify opportunities, threats, and strategic answers in ever tighter time frames. Cognitive diversity can help management teams make the right calls.

However, a key challenge to enabling cognitive diversity on boards is the criteria used to recruit members. On the one hand, the regulator requires skills such as risk and audit to protect customers and investors, but on the other hand we need people with broader experience to enable a board to be cognitively diverse. At the same time, companies need to operate with a focus on making a profit. Some may feel too much diversity of thought can distract from this objective.

To build resilient boards with the strength to meet the enormous challenges we face, particularly as we emerge from the Covid-19 crisis, true breadth of knowledge, experience, and expertise is required. Simply drawing on the expertise of the existing talent pool will not generate the required insights for future risks and opportunities.

To help boards take action now, they should consider setting up shadow and/or youth boards, appointing more junior employees to serve on the board, or hiring advisory directors from very different backgrounds to engage for a shorter period on specific topics and areas.

As a board is not directly involved in the day-to-day management of a business, its greatest input to a company’s development and performance is its cognitive contribution.

It is vital, then, that boards start thinking about how to ensure greater cognitive diversity among its membership. While the board diversity agenda has progressed over the last decade with more focus now on demographic diversity, particularly gender, it’s time for boards to go a step further and make being cognitively diverse their default position.
ABOUT US

Established in 1815, Scottish Widows is dedicated to supporting advisers in the life, pensions, and investments market.

Scottish Widows has been helping people plan for their financial futures for over 200 years. We look after the retirement savings of millions of hard-working people and our role is to help them plan for their long-term financial prosperity. To do this, it's important we continue to use our scale and influence, along with our fund manager relationships, to challenge the companies we invest in on our customers’ behalf to be the sustainable businesses of the future.

It’s our responsibility to use our influence – and shareholder voting rights – to encourage transparency and high-quality governance in the way companies are directed and controlled. This underpins their long-term success and creates shareholder value.

Our priorities for the 2020–2023 period are:

- **Climate & Carbon:** adherence to the Paris Agreement and transition planning for the economy to have net-zero emissions, in accordance with UK law. With a particular focus on those companies which have the highest CO$_2$ emissions.
- **Board Diversity:** better corporate governance through cognitive diversity on company boards.

METHODOLOGY

The starting point for the literature review was the academic journals included on the Finance Times (FT) list of influential scholarly business journals. The list comprises what the FT methodology deems to be the 50 most influential academic management journals. In addition, Corporate Governance and International Review and Group and Organization Management were included due to their clear relevance.

A NOTE ON TERMS

One constraint to our research has been the narrow definition of gender. A lack of disclosure and data collection has resulted in literature being solely focused on male and female board members. We acknowledge gender is not binary for many people and, therefore, the focus is imperfect.

In addition, LGBTQ+ factors are not considered in the research due to a lack of literature on representation of LGBTQ+ people on boards.
ACADEMIC REFERENCES


