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**PAY AT THE TOP: WHEN HR MAKES A
DIFFERENCE**

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EDWARD E. LAWLER III

*Center for Effective Organizations
Marshall School of Business
University of Southern California*

JOHN W. BOUDREAU

*Center for Effective Organizations
Marshall School of Business
University of Southern California*

Executive Summary

Pay at the Top: When HR Makes a Difference

Edward E. Lawler III

University of Southern California

John W. Boudreau, Ph.D.

University of Southern California

Despite its importance, relatively little is known about HR's role in board decision making concerning executive and board compensation and executive succession. To learn more about HR's role, the authors surveyed managers and HR executives in Fortune 1000 firms. Completed surveys were obtained from 106 companies. The Center for Effective Organizations conducted this survey — the fifth in a series that began in 1995. This paper focuses on the most recent data, collected in 2007. The HR elements most strongly associated with board requests for HR help with compensation and succession relate directly to HR's role in strategy formulation, presence in board processes, and contributions to manager sophistication regarding talent and organization issues. Less associated with board help requests are more HR-function-specific elements such as efficiency with resources, use of information technology, technical and consultation skills, and compliance.

Pay at the Top: When HR Makes a Difference

Professor Edward E. Lawler III

Center for Effective Organizations, University of Southern California

Professor John W. Boudreau

Center for Effective Organizations, University of Southern California

Executive compensation and management succession are among the most important issues confronting corporate boards. Decisions in these areas should be informed by valid information and expert knowledge. An obvious source of information and knowledge is the HR function. HR leaders bring unique professional expertise and

perspective to these areas. HR information systems potentially provide unique and relevant data and boards can benefit from an HR contribution that goes well beyond administration and program implementation. However, since the chief human resource officer typically is not on the board, the HR function may not be positioned to influence board decisions regarding compensation and succession. While disciplines such as finance and marketing are routinely included in board decisions, HR may need to be explicitly invited to assist the board, even on topics involving its area of expertise.

Several factors may influence whether HR is invited to work with corporate boards on compensation and succession. HR may already be involved in decisions concerning change management, business strategy and succession planning; all of these have implications for compensation and succession. In addition, the way the HR function is structured, the competence of HR leaders, and the information and knowledge available in HR systems may play a major role in determining HR's role in these decisions.

RESEARCH STUDY

Despite its importance, relatively little is known about what influences HR's role in board decision making concerning executive and board compensation and executive succession. To learn more about HR's role, the authors surveyed managers and HR executives in Fortune 1000 firms. A full report of the survey results is available in Lawler and Boudreau (2009).

Completed surveys were obtained from 106 companies. The Center for Effective Organizations conducted this survey with support from HRPS — the fifth in a series that began in 1995. Surveys have been conducted every three years. This paper focuses on the

most recent data, collected in 2007. It is the first survey to examine HR's role in executive compensation and succession decisions.

WHERE DO BOARDS REQUEST HELP FROM HR?

Table 1 presents the answers to a question about the extent to which corporate boards request help from HR in the areas of executive compensation, executive succession and board compensation. The greatest help is requested in executive compensation. More than 80 percent of HR executives report that their boards request help to a great or very great extent in this area. Executive succession is the area of second greatest requested help. Board compensation is the area where HR is asked for the least amount of help, only 44 percent of respondents report that HR is asked for a great or very great amount of help. This is a significantly lower level of help than for executive compensation and succession ($p < .01$). It may reflect the fact that board compensation tends to be an area where compensation-consulting firms are the major providers of board-compensation information and consulting, not the internal HR staff.

The amount of help the HR function gives with respect to executive compensation is strongly related to the amount of help it gives with respect to executive succession ($r = .48, p < .001$). The level of requested help with board compensation correlates very highly with executive-compensation help ($r = .61, p < .001$) and somewhat less highly with succession help ($r = .40, p < .001$). Overall executive compensation and board compensation help seem to go together, while requested help with board and executive compensation are less strongly related to help with executive succession.

TALENT SOPHISTICATION OF BUSINESS LEADERS

Is the expertise of business leaders regarding the principles underlying human behavior at work, human-capital markets and organization design related to how much boards request help from HR in compensation and succession decisions? Table 2 explores this question, it reports the correlations between business leader and organizational sophistication regarding talent and requested help in the three areas.

The first three columns are questions dealing with how the organization competes for talent overall, whether business leaders outside of HR understand where human capital makes the biggest difference to organization success, and whether their decisions about human capital are as rigorous as decisions about other resources. Board requests for help in all three areas are uniformly and significantly associated with higher business leader expertise and organizational excellence in decisions about talent.

The next four columns in Table 2 focus on business leader expertise in more traditional management areas: business strategy, finance, marketing and technology. The results suggest that business leader savvy, even in traditional and non-HR areas, is related to requests for help from HR. Expertise in all four management disciplines is associated with help requests for executive compensation and succession, while only expertise in marketing and technology is related to requests for HR help with board compensation.

It is interesting that HR help requests are positively associated with business leader expertise in non-HR areas. This suggests that when organizations generally value sound decision-making principles, they may have boards that value specialized functional assistance in all areas. This sets a high bar for HR. If more-expert leaders are the ones

asking for help, the help that HR provides must be rigorous and consistently based on sound and logical principles.

The final four columns show the association between board help requests and business leader sophistication in several specific areas of human-capital management: motivation, development and learning, labor markets culture, and organization design. The pattern is similar to the other management areas; business leader expertise in these human capital areas is consistently related to help requests with executive succession and compensation and often related to help requests with board compensation. The relationships are somewhat stronger for help with executive-succession than for executive compensation, with culture expertise notably more strongly correlated with help with executive succession than with help in the other two areas.

One might expect that if business leaders are more sophisticated in HR areas, they would request less help, but it appears that the more sophisticated business leaders are in human-capital management, the more corporate boards request HR help in compensation and succession. This is good news for HR, because it suggests that as leaders outside HR gain skill in talent and organization effectiveness, they are even more inclined to request HR help. A likely reason for this is that greater business-leader sophistication leads to a stronger appreciation for the value of an HR perspectives at the board level.

The causation may also go the opposite direction. As HR plays a greater role with the board in these three areas, business leaders may realize they must become more sophisticated regarding the decision science of HR.

HR CONTRIBUTION TO LEADER DECISIONS

If more sophisticated business leaders request more help, does that mean that the manner in which HR contributes to talent and organization decisions affects the help that is requested by boards? Table 3 shows the association between board help requests and specific ways that HR contributes to talent and organization decisions. The first two columns show that help requests in all three areas are significantly and positively related to the degree to which HR leaders identify unique strategic connections between human capital and business strategy, and have a good understanding of how and why those human-capital connections create strategic differences. The relationships are stronger for executive compensation and succession, but they are significant for board compensation as well.

The next two columns show low, mostly insignificant associations, suggesting that the degree to which HR educates business leaders about their talent decisions, and the degree to which HR adds value through compliance do not relate to board help requests. With regard to educating business leaders, at present, this may be an underappreciated HR role by business leaders and boards. Notably, it is significantly related to executive-succession help requests, suggesting that in at least this area, HR's ability to educate business leaders has some effect on how boards use the HR function. With regard to compliance, the finding of no relationship seems logical, because compliance with rules, regulations and laws is very important, but only gets board attention when something goes wrong.

The final two columns show uniformly strong associations between help requests, and the degree to which HR adds value through high-quality program delivery and

through improving talent decision making inside and outside the HR function. This suggests that even at the board level, HR benefits from increased quality in its more traditional role of delivering services. Unlike compliance, it appears that service-delivery value is not simply a minimal expectation, but something that gets board attention.

The results for HR adding value through improving decisions are also encouraging. They suggest that when HR is effective in decision-support overall, it is more involved in succession and compensation at the board level.

HR'S ROLE IN STRATEGY

The HR function's role in forming and implementing corporate strategy varies significantly from essentially no role in some firms to a full partnership in others. Table 4 shows the relationship between HR's involvement in strategy and its role in executive compensation, board compensation and executive succession. The correlations are particularly high for executive compensation and executive succession. There is also a statistically significant relationship with board compensation, but the relationship is relatively weak.

HR is likely to possess the information and expertise needed to ensure a fit between business strategy and how executive positions are filled and compensated (Lawler 2008). Thus, finding strong relationships with executive compensation and succession is not surprising. It probably reflects causation that goes in both directions. That is, when HR achieves a stronger role in strategy, it is likely to have both the presence in the strategy process, and the understanding of strategy decisions, such that it is invited to advise on how to structure executive compensation and succession. It may also be the case that when HR is requested to be involved in executive succession and

compensation at the board level, that role opens the door to a stronger role in strategy formation.

The correlation between the help requested for board compensation and HR's role in strategy is positive and significant, but lower than the correlation for executive succession and compensation. This may reflect that the board compensation is less directly connected to strategy than executive compensation or executive succession. HR's help with board compensation may more closely reflect the degree to which it has the position of a trusted advisor to the board, whereas executive succession and compensation may reflect a specific need for help in structuring and designing executive rewards that align executive interests and strategy.

Having found positive relationships between HR's overall role in strategy, and the extent to which it is asked for help in the three areas, it is important to explore how help with these three areas is related to HR involvement in specific business-strategy activities. Table 5 shows the relationship between the degree to which HR engages in five important business-strategy activities and the degree to which it is asked for help with executive compensation, board compensation and executive succession.

The results show positive and significant correlations between all strategy activities, with executive compensation and executive succession, but only one significant one with board compensation. The one significant correlation for board compensation concerns HR engaging in "work with the corporate board on business strategy," and may reflect the earlier observation that when HR is present in board deliberations, it is also asked for input on board compensation. Still, the overall

conclusion is that HR strategy activities associate far less with requested help with board compensation than with executive succession and compensation.

The correlations related to executive succession and executive compensation show positive relationships to all the strategy activities, whether the role is to assess organization readiness, implement strategy, help decide on options already identified, or identify the options themselves. All three correlations with the item asking about working with the board on strategy are significant. This most likely reflects the reality that when HR has a presence in working with the board on strategy, its presence enhances HR's role in helping with executive succession and compensation as well as board compensation.

HR STRATEGIC CONTRIBUTION

How HR contributes to a corporation's strategy is strongly related to the extent of help requested in: executive compensation, board compensation and executive succession. Table 6 presents data on the relationship between four characteristics of the HR contribution to strategy and the help requested from HR by the corporate board.

The more HR is a partner with the line in developing the business strategy, and the more the human-capital strategy is integrated with the business strategy, the more the board asks HR for help with executive compensation, board compensation and executive succession. The highest correlations are with executive succession. The most likely explanation is that when HR works on business-strategy development and ties it to the HR strategy, HR becomes well positioned to help design and implement compensation and succession plans. HR is not only likely to know what the plans need to do; it has the visibility and relationship necessary to help get it done.

The degree to which HR drives change management is also highly correlated with whether corporate boards ask for HR help. This too is to be expected since for change management to be successful, the right reward and succession practices need to be in place. Finally, HR making rigorous data-based decisions about human-capital management is strongly correlated with help on executive compensation, board compensation and executive succession. Again, when the human-resource strategy is tied to the business strategy and tied to rigorous data-based decisions, HR is in a well-informed and knowledgeable role about how executives and board members should be compensated, and about executive succession.

Across the board, the greater the extent to which HR contributes in all of these strategy areas, the more boards request help. Unlike some previous results, the pattern is also strong for board compensation, not just for executive compensation and succession. This suggests that a wide variety of avenues toward strategic contribution may either enhance HR's desirability as a partner in board deliberations, or that when HR is asked for help in all of these areas, their capability to contribute in all three ways increases. It is probably some of both. However, the authors believe — in this case — the most compelling logic is that if HR can contribute to strategy in these ways, it creates a demand for their help at the board level with respect to succession and compensation.

BOARD REQUESTS FOR HELP

Are the contributions that HR is asked to make to boards in other areas related to the request it gets for help with compensation and succession planning? HR can be asked to the board in areas such as addressing strategic readiness, change consulting, developing board effectiveness/ corporate governance, and providing information about

the condition/capability of the work force. One possibility is that requests for help with compensation and succession issues are unrelated to requests for help in other areas. Or, it may be that it is one of many areas where boards either do or do not ask for help from HR. If requests for help are correlated, it suggests that requests for board help with succession and compensation may be more a function of HR's general presence and active engagement with the board, than because of HR expertise in specific compensation and succession-planning decisions.

Table 7 shows the correlations involving requests for help in four areas. They are all significant, and generally high. They argue strongly for the conclusion that board requests for HR help with compensation and succession are related to a wide variety of HR board requests for help. This suggests that when HR is asked to do compensation and succession work with the board, it is also asked to help in other areas. It appears that boards develop a general tendency to request help from HR, rather than limiting themselves only to specific expertise related to succession and compensation decisions.

STRUCTURE OF HR

During the past several decades, organizations increasingly have moved toward organizing HR functions with service centers and centers of excellence. These centers provide expertise and administrative support and usually are complemented by placing HR executives in the organization's various business units or departments. This design is intended to provide subject-matter expertise in key HR areas as well as responsive, efficient and effective HR services. If these structural elements indeed create a more responsive and efficient HR function, boards should tend to rely more on HR expertise when they are present. Recall the earlier finding that the value HR delivers through

services and practices was strongly related to requests for HR help from the board. It also is possible that once HR is organized in this way, it frees the HR function to focus on strategic considerations.

Table 8 shows the relationship between the existence of centers of excellence and HR's help with executive compensation, board compensation and executive succession. All the correlations are statistically significant and support the argument that centers at the corporate level help insure that HR has the expertise it needs to deal with corporate strategy and the decisions that must be made at the corporate level. Executive compensation and succession decisions affect all organizational units, so one would expect that creating corporate centers would provide the opportunity for HR to have the cross-unit perspective that is needed to help with compensation and succession.

Two other features of the HR organization shown in Table 8 are insignificantly correlated with boards requesting HR help: The efficiency with which the HR organization is run, and the degree to which information technology is used. The result for resource efficiency is not surprising as it is not directly related to executive compensation, board compensation and executive succession.

The result with respect to information technology is surprising as IT can be a vehicle for providing the information needed to make sound compensation and succession decisions. This result may reflect that information technology can serve a wide variety of purposes, and contain and generate information ranging from HR processes and workforce attributes to business outcomes. The mere presence of IT does not necessarily mean that information aimed at assisting with these board-level decisions is available.

HR SATISFACTION WITH ITS SKILLS

There is increasing attention to developing the skills of HR executives (Boudreau and Ramstad 2007; Ulrich, et al. 2008). One can divide HR skills into three major categories: Technical skills reflecting the professional knowledge required to design and deliver key HR programs and practices; business skills reflecting HR's understanding of business disciplines and the specific business issues and initiatives; and consulting skills reflecting the capability to advise, coach and provide useful diagnosis and perspectives (Lawler, Boudreau and Mohrman 2006). Table 9 shows the relationship between board requested help and the satisfaction of HR leaders with the HR functional skill level in three categories.

Interestingly, HR satisfaction with HR technical and consultation skills is not significantly correlated with board requests for HR help with compensation and succession decisions. Satisfaction with business understanding is related to requests for help with board compensation and executive succession, but not executive compensation. This pattern may reflect the fact that HR's technical skills and consultation skills reflect a capability that is applied at many levels of the organization, but is not critical to dealing with the board on these issues. It is probably not that boards don't value such skills, but they may not feel they are related to the help they need with compensation and succession. The level and quality of business understanding, on the other hand, is directly related to the issues that boards confront in compensation and succession decisions and thus it is significantly correlated with being called on for help.

CONCLUSION

What aspects of HR are associated with board requests for assistance with executive and board compensation and executive succession? The data suggest that the most strongly associated HR elements are those relating directly to HR's role in strategy formulation, presence in board processes, and contributions to general-manager decision sophistication regarding talent and organization issues. Less associated with board help requests are the more function-specific elements of HR such as efficiency with resources, use of information technology, technical and consultation skills, and value added through compliance.

The results presented in this paper are correlational results, so the direction of causation cannot be fully determined. It may be that an HR presence and involvement in board decisions concerning compensation and succession leads to the visibility and respect necessary to build a broader role in contributing to strategy. Alternatively, it may be that when HR organizations successfully build their capability to contribute to strategic decisions, they are invited to help with board-level decisions concerning compensation and succession. Likely, both occur. Regardless of whether it starts with a presence at the board level, or with a strong strategic and decision-support role more generally, HR organizations that can achieve a stronger strategic and decision-support role are more likely to be invited to assist boards in these important areas.

While most HR strategy and decision-support elements are associated with all three board help-request arenas, HR help is requested more often with executive succession and compensation, than with board compensation. The associations between HR strategy and decision support are also stronger in the two executive areas than in the

board compensation area. This may be because executive-succession and compensation decisions are more clearly tied to HR's success in improving organization processes, while board compensation is often distinct from those processes. Still, the results suggest that it is common for HR to be asked for help with board compensation, and that greater strategic capability and decision-support contributions by HR improve the chance that boards will look to HR for assistance in this area.

IMPLICATIONS FOR HR

What should HR organizations do in light of these findings? There are a number of actions that should be taken. Perhaps the most obvious one is to create structures at the corporate-level that support board-level decision processes and develop expertise in business strategy. Excellence in the administrative and function-specific aspects of HR add value, but board involvement with HR apparently depends more on HR elements that create a specific presence in corporate-decision processes (such as having corporate-level centers of expertise and a specific role in ongoing corporate and board strategy processes). HR organizations would also do well to incorporate board-level experience into the career paths of HR leaders, accelerate the progression of the HR function from a strictly compliance-based paradigm toward more decision support, and generally enhance HR's role in strategy-formulation and design.

Finally, HR should enhance the talent and organization decision-science knowledge of business leaders, because board help is related to the sophistication of business leaders. HR has much to contribute by bringing principles of human behavior, organization effectiveness and labor markets to the deliberations of boards regarding executive and board compensation and succession. To tap that potential contribution,

boards must more frequently request HR's help, and HR must evolve to be prepared to deliver on those requests through a stronger presence and capability in delivering strategic insights, decision support and unique value.

HR can certainly achieve a strategic partnership in many ways besides contributing to board decisions concerning succession and compensation, but HR's role with the board in these areas is important to HR's overall role. It represents an important business area and is a symbolic indicator of HR's status. As a result, it deserves attention and continuing scrutiny by HR executives.

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AUTHORS

Edward E. Lawler III is the Distinguished Professor of Business and director of the Center for Effective Organization in the Marshall School Business at the University of Southern California. He has been honored as a top contributor to the fields of organizational development, human-resource management, organizational behavior and compensation. He is the author of more than 300 articles and 43 books. His most recent works include *Talent: Making People Your Competitive Advantage* and *Built to Change: How to Achieve Sustained Organizational Effectiveness*, which was coauthored with Christopher G. Worley. *BusinessWeek* proclaimed Lawler one of the top six gurus in the field of management, and *Human Resource Executive* called him one of HR's most influential people. National television appearances include The Today Show, CNN, MSNBC and CNBC. For more information, visit <http://www.edwardlawler.com> and <http://ceo-marshall.usc.edu>.

John W. Boudreau, Ph.D., is Professor and Research Director, University of Southern California's Marshall School of Business and Center for Effective Organizations. He is recognized worldwide for breakthrough research on human-capital strategies. His research has received the Academy of Management's Organizational Behavior New Concept and Human Resource Scholarly Contribution awards. Dr. Boudreau is a Fellow of the National Academy of Human Resources. He has published over 50 articles, books and chapters, including a leading textbook in HR. His most recent works include *Beyond HR*, co-authored with Peter M. Ramstad, and *Investing in People* co-authored with Wayne F. Cascio. He has held leadership positions in the Academy of Management, the Human Resource Planning Society, WorldatWork, the Society for Industrial and Organizational Psychology, and the California Strategic HR Partnership. For more information visit <http://marshall.usc.edu/ceo/members/john-w-boudreau.htm>

TABLE 1 WHERE BOARDS REQUEST HR HELP

	Percentages					
How much does your Corporation's Board call on HR for help with ...	Little or No Extent	Some Extent	Moderate Extent	Great Extent	Very Great Extent	Mean
Executive compensation	5.2	5.2	6.2	40.2	43.3	4.1
Board compensation	21.3	11.7	23.4	28.7	14.9	3.0
Executive succession	10.3	6.2	18.6	23.7	41.2	3.8

TABLE 2 RELATIONSHIP BETWEEN BUSINESS LEADER TALENT SOPHISTICATION AND BOARD HELP

DECISION MAKING											
How much does your Corporation's Board call on HR for help with ...	We excel at competing for and with talent where it matters most to our strategic success	Business leaders have a good understanding about where and why human capital makes the biggest difference in their business	Business leaders' decisions that depend upon or affect human capital (e.g. layoffs, rewards, etc.) are as rigorous, logical and strategically relevant as their decisions about resources such as money, technology and customers	Business leaders understand and use sound principles when making decisions about:							
				Business Strategy	Finance	Marketing	Technology	Motivation	Develop-men & Learning	Culture	Organiza-tion Design
Executive compensation	.35***	.31**	.31**	.24*	.26*	.37***	.28**	.26*	.23*	.18	.22*
Board compensation	.33***	.30**	.35***	.17	.12	.27**	.24*	.23*	.26*	.16	.18
Executive succession	.25*	.29**	.29**	.34***	.24*	.30**	.31**	.38***	.41***	.39***	.36***

Significance Level: * $p \leq .05$ ** $p \leq .01$ *** $p \leq .001$

TABLE 3 RELATIONSHIP BETWEEN HR DECISION CONTRIBUTIONS AND BOARD HELP

HR DECISION CONTRIBUTIONS						
How much does your Corporation's Board call on HR for help with ...	HR leaders identify unique strategy insights by connecting human capital issues to business strategy	HR leaders have a good understanding about where and why human capital makes the biggest difference in their business	HR systems educate business leaders about their talent decisions	HR adds value by insuring compliance with rules, laws and guidelines	HR adds value by delivering high quality professional practices and services	HR adds value by improving talent decisions inside and outside the HR function
Executive compensation	.37***	.44***	.16	.02	.29**	.39***
Board compensation	.28**	.23*	.18	.04	.28**	.28**
Executive succession	.44***	.45***	.25*	.01	.30**	.49***

Significance Level: * $p \leq .05$ ** $p \leq .01$ *** $p \leq .001$

TABLE 4 RELATIONSHIP BETWEEN HR'S ROLE IN STRATEGY AND BOARD HELP

How much does your Corporation's Board call on HR for help with ...	HR'S ROLE IN STRATEGY [±]
Executive compensation	.46***
Board compensation	.21*
Executive succession	.46***

Significance Level: * $p \leq .05$ ** $p \leq .01$ *** $p \leq .001$

[±]Response Scale: 1 = No Role to 4 = Full Partner

TABLE 5 RELATIONSHIP BETWEEN BUSINESS STRATEGY ACTIVITIES AND BOARD HELP

How much does your Corporation's Board call on HR for help with ...	BUSINESS STRATEGY ACTIVITIES				
	Help identify or design strategy options	Help decide among the best strategy options	Help plan the implementation of strategy	Assess the organization's readiness to implement strategies	Work with the corporate board on business strategy
Executive compensation	.30**	.30**	.23*	.43***	.41***
Board compensation	.10	.14	.13	.17	.21*
Executive succession	.38***	.37***	.34***	.43***	.49***

Significance Level: * $p \leq .05$ ** $p \leq .01$ *** $p \leq .001$

TABLE 6 RELATIONSHIP BETWEEN HR STRATEGIC CONTRIBUTION AND BOARD HELP

How much does your Corporation's Board call on HR for help with ...	HR STRATEGIC CONTRIBUTION			
	Partner with line in developing business strategy	A human capital strategy that is integrated with business strategy	HR drives change management	Makes rigorous data-based decisions about human capital management
Executive compensation	.40***	.42***	.46***	.38***
Board compensation	.25*	.31**	.28**	.28**
Executive succession	.54***	.57***	.48***	.44***

Significance Level: * $p \leq .05$ ** $p \leq .01$ *** $p \leq .001$

TABLE 7 RELATIONSHIP AMONG REQUESTS FOR HR HELP

How much does your Corporation's Board call on HR for help with ...	BOARD REQUESTS FOR HELP			
	Addressing strategic readiness	Change consulting	Developing board effectiveness/ corporate governance	Information about the condition/ capability of the work force
Executive compensation	.43***	.37***	.36***	.42***
Board compensation	.27**	.31**	.48***	.37***
Executive succession	.58***	.49***	.40***	.56***

Significance Level: * $p \leq .05$ ** $p \leq .01$ *** $p \leq .001$

TABLE 8 RELATIONSHIP BETWEEN HR ORGANIZATION AND BOARD HELP

	HR ORGANIZATION		
How much does your Corporation's Board call on HR for help with ...	HR Centers	Resource Efficiency	Information Technology
Executive compensation	.39***	-.02	.16
Board compensation	.27**	-.06	.13
Executive succession	.32***	-.02	.20

Significance Level: * $p \leq .05$ ** $p \leq .01$ *** $p \leq .001$

TABLE 9 RELATIONSHIP BETWEEN HR STAFF SKILLS SATISFACTION AND BOARD HELP

How much does your Corporation's Board call on HR for help with ...	HR STAFF SKILL SATISFACTION		
	HR Technical Skills	Business Understanding	Consultation Skills
Executive compensation	.03	.11	.03
Board compensation	.05	.26*	.06
Executive succession	.08	.21*	.06

Significance Level: * $p \leq .05$ ** $p \leq .01$ *** $p \leq .001$