Kumar Mangalam Birla To M Damodaran: Chairman And MD Roles Should Be Separate

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Kumar Mangalam Birla has backed the regulator's decision to split the roles of chairman and managing director, breaking ranks with some of the big names of India Inc. on this contentious issue.

"We have for the longest time had separation of MD and chairman, as two separate roles," Birla said of his own business group, in a conversation with M Damodaran, former chairman of the Securities and Exchange Board of India, at the inaugural session of a two-day conference titled *Gatekeepers of Governance*.

"I can't imagine how it would be like to have both of those roles combined into one. The difference in the roles is very stark."

That's a contrarian view as India's industry bodies have written to the Finance Ministry seeking a review of SEBI's decision asking companies to split the role by March-end, citing that 90 percent of the companies are family-run. Rahul Bajaj, chairman of Bajaj Group, and Venu Srinivasan, chairman of TVS Group, recently criticised the new norm, calling it a western concept and completely out of sync with ground realities in India.

Birla, however, said having a chairman also means that the company has access to someone who is above the management in case there are issues that require resolution. "For me, this whole concept is something that is a given."

> **I think that it would be quite ironic to have both functions carried out by the same person. Chairman and chief executives should not be related. I dread to be in a situation like that. It would**

be an extremely complex situation to deal with. There are many family run companies which have a situation like that but the dynamics are very different.

Kumar Mangalam Birla, Chairman, Aditya Birla Group

When Damodaran cited instances of the two positions being occupied by family members, say father and son or brother and brother, Birla quipped - “As you would know in our context, we are very fortunate not to have brothers.”

Whistleblower Complaints

Birla also said there’s a need for guidelines on anonymous complaints. “You need clearly articulated guidelines as to whether there can be anonymous complaints,” Birla said in conversation with Damodaran. “Do they (such complaints) have to be accompanied by the name of the complainant, is it only about salary, misconduct?”

Whistleblower complaints about lending practices at ICICI Bank Ltd. led to an investigation into the allegations of quid pro quo against the private lender’s former head, Chanda Kocchar. An anonymous complaint was also at the heart of Infosys Ltd.’s founders’ quarrel with the software services provider’s former Chief Executive Officer Vishal Sikka, who eventually quit. Infosys recently was once again mired in controversy after another whistleblower letter came to light alleging poor accounting practices under new CEO Salil Parekh.

Birla advised caution while investigating such complaints. “Whoever the compliance officer is has to use his judgment. You can’t run after every complaint, because that will become a wild goose chase,” said Birla, who heads the textile-to-aluminium Aditya Birla Group. “Companies need someone who has the advantage of wisdom over others in the company to pick up the right complaints, and bring it to the notice of the right people in the company.”

“ **You can’t ignore them (whistleblower complaints), but you’ve got to be careful not to start chasing ghosts because that can be quite a counter-productive thing to do.**

Kumar Mangalam Birla, Chairman, Aditya Birla Group

M Damodaran (left) and Kumar Mangalam Birla at the Gatekeepers of Governance conference. (Photo: Jyotiprakash Rout/BloombergQuint)

Succession Planning

Birla doesn't think most companies adequately plan for succession of top executives. "I don't think we have a system of discussing succession planning for the next five years, and I doubt most Indian companies do," he said. "I think a lot of us don't even do it (succession planning) internally, leave alone taking it to the board."

On how corporate India should look at this seriously, he put the onus on the CEO and chairman.

> **" You could mandate that succession planning is discussed at the board once a year for example, but the quality of discussion depends very much on the chairman and CEO; on how well planned they are and also, how much they value the opinions of the board members, especially the independent directors.**
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> **Kumar Mangalam Birla, Chairman, Aditya Birla Group**

Proficiency Test For Directors

Concerns about corporate governance at Indian companies have prompted the government to introduce a proficiency test for independent directors. Birla, however, doesn't see that as a solution.

"Sometimes innovation is not required, and we must stick to the trusted old ways that have come down with time," he said. "It depends on the person's track record, whether experience is relevant to the company's operations and strategies."

A test for integrity, I don't think exists. Any other test is a functional test. It's more about the track record and the experience.

Birla was speaking at the inaugural session—called *Looking Forward, Looking Back*—of the *Gatekeepers of Governance* conference hosted by Damodaran. Among the issues discussed were:

- Handling of whistleblower complaints
- Separation of roles of chairman and chief executive
- Relevance of the proficiency test
- Role of independent directors on boards
- Succession planning, or the lack of it

Read the edited transcript here…

M Damodaran: Two distinguished leaders of corporate India have trashed the proposal to separate the position of the chairman from the chief executive and I am referring to Mr. Rahul Bajaj and Mr. Venu Srinivasan, both of whom were reported as saying that this is completely out of sync from the ground realities in India and that we should not be separating. They say these are western concepts that are being imported into India etc.. I know for a fact that there are corporate leaders in this audience who subscribe to the same view. But I know equally that there are also people who strongly believe that the opposite is true. What are your views on this?

Kumar Mangalam Birla: We have for the longest time, had the role of MD and Chairman- two separate roles so I cannot imagine how it would be like to have both of those roles combined into one. The difference in roles is very stark, the chairman obviously is looking at the broader context, the GDP issues, strategic directions. He is also looking at heat-risk maps to see how the company could get impacted by the external environment and what is happening in the world around. The MD primarily, his/her role is to focus on a day-to-day, month-to-month or yearly focus and escalate issues that are agreed upon in advance to the chairman. Having a chairman also means that you have access to someone who is above the management, in case you have an issue that requires resolution on his or her level. So, for me, this whole concept is something which is a given. I don't know how we would function with the MDs and the company's role put together, amalgamated. I think it would be quite ironic to have both functions carried out by the same person.

There are elements to this which are facing an even bigger pushback. But of course, it's the basic question of separation. Then there are two elements. Should the chairman be non executive. I suppose, if you separated follows from the chairman, because you cannot have a managing director who is non-executive. I would hate to a company that has a non-executive managing director. So that follows from the separation but the third which is where I am hearing that corporate India is pushing back a lot is the proposition that the chairman and the chief executive should not be related. India is the first to prescribe something in this nature; this prescription doesn't exist anywhere else in the world. The chairman and the MD should not be related to each other- father and son, mother and daughter, father and daughter, brothers maybe…they shouldn't be related.

As you would know in our context, we are very fortunate not to have brothers.

That is why I am asking you this question because you can take an objective view, you don't have to be defensive.

Having said that, I'd dread to be in a situation like that. That would be an extremely complex situation to deal with, I would imagine. I am sure there are many family-run companies in India which have a situation like that, and I guess the dynamics would be different. I see that the concept of family counsels has increased in India where you have independent people advising families as to how to sort out any potential or existing conflict. As far as we are concerned, since I am the only one from the family who actually runs a business, every company would have an MD and a chairman who are not related. In fact, as a philosophy, if two people are related, they can't work in the same function for sure any company. They cannot be in the same line of authority and likely not to be in the same, say finance function, unless they are separated in terms of part of the function.

The other issue, which is very current, is the prescription of a proficiency test for independent directors. An independent director, no matter what his/her background is, qualification is, has to pass a proficiency test which comprises of a paper and securities law, securities and company law and paper and basic accountancy. Once you pass, you get 60 percent in that, then it is believed that you are God's gift to the corporate courtroom and that you add value. It is prescribed, it is ready, some people are writing out the question papers. I hope they don't make it too difficult. Again, like you spoke about the separation because you could speak about it objectively, I can also speak about this objectively because those who have done more than 10 years on board, are exempted. So, I am 10+ and I don't have to prove whether I know this or not. I was joking to someone that my successors in SEBI- who headed SEBI after I did, and have therefore less than 10 years, would have to take examinations in securities law in order to stay on board. Is this the answer on getting better directors on boards?

Not at all. I think the things you are talking about are all functional knowledge.

India is the first country to do it.

Sometimes, innovation is not required. At times you stick to the trusty, old concepts that have come down over time. I think its more about a person's track record, his experience, whether his experience is relevant to a part of the company's operations. If not, generally overall to the space that the company operates in terms of strategy. If one of our company's product mix is changing and the auto players are going to become more and more important as a customer segment, we are looking for a director who has experience in the auto segment because that's a segment that's new to us. Some of our directors have held the position of CEOs and have had an outstanding record of running companies. Some are specialists, in some cases depending on the requirement of the company in terms of input. I don't think a test for integrity exists. Any other test is a functional test I don't either you or I or more senior people in this room would remember everything about security law and I don't think that is required either for someone who is on the board. I think its more about track record and the experience. In fact, its relevance to the company that you're appointing he/she on the board.

You have some very distinguished directors on your board including a distinguished global management guru who I understand is in the city today. I don't know whether he has done 10 years. His advice is to the top corporations of the world is, to run the businesses and been on the boards. He has written books that are global bestsellers. I haven't checked whether he has done 10 years to get the exemption but staying on the subject of independent directors, there is one school of thought which believes that overtime, this category has not added value to the board, therefore, it is completely dispensable. There is another category which believes that you've got to empower them to be stronger in the boardroom than they are at this point of time. Do people like this need external props to empower them? Aren't they adequately empowered if they see themselves empowered? Or do you see your independent directors not contributing what they should be contributing?

I would like to think that there is a mixed-bag. I mean, there are some who don't really bring much to the table. There are many others who not only bring their experience to the table, but they will go out of their way to research or talk to people on topics that the board has issues with. Many of them play a very effective role of being a conscience keeper to the company. I think that in itself is a very important contribution that many of them make. I think their role in committees is normally very useful; whether it is the audit committee or the finance committee or the nomination or the numeration company, I see that we get some very valuable insights from several of them on these committees. These committees are empowered. A lot of the things that independent directors talk about, suggest and actually get implemented in a very institutionalised kind of a way. I think the idea of not having independent directors is now a very alien idea in India. There was a time where you did not require independent directors up until the mid-80s I would think. Then there are sort of layers to it in several of my contemporaries. Global companies also have on their board the concept of a lead independent director and his/her role is in a sense given more sense onerous him/her or on the company. So, I think while we are a little away from getting into that kind of nuanced segregation of roles, the question of having independent directors is under debate anymore.

The third issue which is again, in the headlines of the last few days is the whistleblower complaints. This is relatively new in India. It was a non-mandatory provision for some time. After that, some companies introduced it but now, everybody is required to have it. It's a fairly mixed bag. In theory, a good instrument- is it playing out well in practice? Is there a lot of pressure on companies because whistleblowers have disproportionate power in the way this scheme is structured? What are your thoughts on that because there's a recent case that has raised the issue of what constitutes timely disclosures in the exchanges of the whistleblower complaints is received?

Again, it's a mixed bag. I mean, you need to have in my view, very clearly articulated guidelines as to, can there can be anonymous complaints, do complaints have to be accompanied by the name of the complainant, can it be a complainant where it is about just salary or wages or increments? So, and so is about misconduct or not complying with companies' values. I think one has to use one's judgement; whoever is the compliance officer has to seep through that and you can't run after every complaint because that would become a wild goose chase but I think you need someone who has the judgment and who also has the advantage of and the wisdom of others in the company to pick up the right ones and to bring it to the notice of the right people in the company. So, I say, you can't ignore them, but you got to be careful not to start chasing ghosts because that could be quite the counter productivity.

There is another issue which holds the solution to some of this. That is the issue of board evaluations. What is your view on board evaluations? You had this for the last few years now and my experience is that, in most companies, every director gets 11 out of 10 after peer evaluation and yet it used to be said in the service to which I belong that in one state of the Indian Union, a fairly large popular state. Everybody was graded outstanding and the explanation was, they were always standing outside the room so they must be outstanding guys. So, our board evaluations remind me of that kind of an evaluation system. It's prescribed, people are going through the motions, it is not adding up to anything. Is there a way that we can breathe life into this?

So, in my experience, and in our companies, four or five years ago, everyone was graded an A or an A+ and now, I see some distinction happening- in the sense that you would have bought members who would, say, all independents average, all executives outstanding, and another category could do much better. So there is some distinction which is starting to happen and I think that hesitance to actually call out performance is diminishing but taking a very long time. I have always had ten on ten, as you can imagine, as a chairman of all my companies which is somewhat disappointing because that doesn't mean anything to me at all. I'd love to get some feedback either formally or informally. So I think it's seen as of today as a statutory exercise that every company has to go through.

Do you think we will see a time that on the basis of evaluation, some director will be told "Thank you very much but maybe you should spend your time elsewhere rather than be on this boat".

I don't see that happening for a very long time.

Is it a cultural issue or is it that having got somebody on the board, we think that we made a mistake and if we persuade the gentleman or lady to leave, we are admitting that we failed in the first instance getting that person?

I think that's a cultural issue and the fact that the mandate of this audit is to give people feedback on how they are doing in terms of their role as a board member. So, that they can get objective feedback and they can contribute more on their specific areas in which they can contribute. Either the chairman or MD needs to set the agenda let's say, for board meetings more clearly, take charge of discussions, make sure that you are getting the right inputs and the right areas of focus from the committees. So, I think that's more that kind of a role where the objective is to improve the productivity of the discussion of the members and get more participation from all the members on the board. I don't think that its meant to be used as a mechanism where you actually ask the director of the board to actually leave the company.

It's interesting you say this because schedule IV which talks about evaluation of the companies act says, at the end of the valuation, a decision should be taken whether the director should go or stay and my problem with that has been that, evaluation doesn't mean black or white. Somebody has some strength, somebody has some areas of improvement, so you point to that person that this is the areas we want you to spend more time, more quality time maybe read up more, maybe speak up more in board meetings. Something like that.

We do have meetings twice a year only of independent directors who meet by themselves and come back and give feedback to management. That's more about what's the strategy of the company and vision of where we are going, what we need to do more of, what we need to avoid, that sort of things. I think that is also recent in the last two or three years. That I found is very recent in the last two or three years and it is a value-adding exercise. They have sometimes the context of management or asset promoters being so close to the company and its operation that they might have just hit a blind spot. I think that's a very valuable contribution that independent directors can make.

This is a another very important issue and it is related to one of the issues that I raised earlier which is, are corporate boards paying enough attention to succession planning? I know it's being talked about a lot, about 10 or 15 years ago, I was at a meeting with a few people from the industry and when I raised the raised the topic of successional planning, it was an informal discussion and I understood for the first time, I understood what pin-drop silence meant when I mentioned succession planning. So, things have moved on, there are companies that are addressing it is enough at the level of the CXOs, at the level of the MDs, the KMPs- are these being thought through?

We are at stage where when there is a need for a change, whether someone has been asked to leave on account of performance or there is retirement happening, at that point of time, we would bring several profiles to the NRC to start with who would then recommend to the board and we will have a very extensive discussion around at least two or three different profiles so hopefully, one from outside, two from inside is a kind of metric that we kind of want to follow. I don't think that we have a system of discussing succession planning for the next five years and I doubt that most Indian companies do well. I think that a lot of us don't do it even internally leave it alone taking it to the board.

The real problem area in succession planning is when you have a promoter managing director and leaving ones position doesn't come most easily in India even if you are an executive chairman or

non-executive, it doesn't come easily to people. We have seen several instances of people who want to stay on, we've seen instances of people who want to redefine what non-executive meant even as they make the transition. So, we have lived through all of those problems. How do you ensure that corporate India looks at this a little more seriously? Mandating is not the answer. Is there some other way because succession planning is serious, and I don't think it's getting enough attention there.

In particular, on succession planning?

Yes, succession planning. How does one ensure that, that gets attention and streamlined? Not that one person is forward looking, is let's say, more understanding to the future needs of the company and therefore does it but if he/she goes, the next person says this is the matter of minor detail my job is to run the business. So, how do ensure that the good system is put in place for this?

To be discussed at the board? I don't think you can ensure a quality standard of discussion you could mandate that succession planning is discussed at the board once a year for example and once in two years which means it will find a place for the meeting but the quality of discussion can't be mandated and that depends very much on the chairman, CEO on how well planned they are and also, how much they value the opinions of the board members especially the independent board members.

Another major area which has been neglected for many years but has been talked about for the last few years is risk management. Are boards today equipped in terms of their understanding of the business, in terms of understanding of the wide range of risks. To look at risk management. Because I know in some companies there is this issue of managements taking the position that we understand risk and independents on the board don't understand risk and therefore, we address risk and you stay out of this. There are also companies where independent risk directors lead risk management committees to the board in order to address this in a somewhat dispassionate way. Do you think we have enough capacity in the boardroom to address this?

Some of the board companies that we have, have a risk management committee, not all do. But I think that it's something that management has to track and has to track in a very systematic way. We have something that we call the risk heat map where we segregate risks into four different quadrants depending on the possibility of those actualising and the impact of those which is discussed at a management level every quarter. But I think it's important as part of the induction of a director to apprise him or her of the different risks that a company is exposed to, whether it's technology risk whatever the risk might be from a competitive landscape point of view. It's important that the management, the CEO keep the board apprised of developments on that front. We would see a heat risk map at least twice a year in the board where the CRO- the chief risk officer if not the CEO, would talk about any movements within the risk map. So for example, we in Novelis which is an aluminium rolling company, we figured out from seeing the heat risk map that there is a new technology that steel is developing—the lightweight steel. The main advantage of aluminium versus steel is that it's much lighter and we figured from there that that wasn't something that had been highlighted by the management to the board. We picked that up as being a very important criteria for competition in the future which in turn gave way to series of developments. We're now taking that as a very important exercise project in our development centre and I think about a couple of hundred million dollars have been spent because that is protecting your competitive advantage as aluminium vis-à-vis steel. So I think how you interpret a risk heat map becomes a very important element and also it can be a tool that can be very useful in terms of providing information that sometimes would have not just made it to the radar.

Your group has been very active in the CSR space. Long before CSR was mandated, or talked about, you've been doing what today is called CSR. If you look at the journey of CSR, initially, came the voluntary code of conduct. In the Companies Act, it was the only provision where they said comply or explain. There were no penal consequences attached so that you had to go and explain shortfalls to shareholders. Then, the ministry decided that comply or explain meant explain to the ministry not explain to the shareholders. So, you imported a concept from Britain but switched it to me, explained to the ministry in terms of shortfalls and they very quickly compiled a list of all of those who were below that percentage and what the amounts were clearly intended to go into the general coffers I imagine or some such thing. Now, we are finding further changes in the CSR

prescriptive range but do you think firstly it ought to have been mandated? So, I've always believed that CSR is an affair of the heart not an accounting entry, it's not about percentages. It is what you believe to be right and you do that. It doesn't matter if you are short by a few hundred rupees or excess by a few hundred doesn't matter. But the swings now that you have on CSR, I think over the last one year itself there have been two major changes in the policy framework is that the way we should be looking at CSR.

I actually think it's worked out quite well. So, you always have in the case of a new concept like CSR, there will be some amount of abuse which I'm sure exists but I find that a lot of companies, whatever is the amount that it works out to, actually are looking out to contribute even if in a small way very often to a cause that is dear to the employees of the company or to an initiative where some of the employees would like to spend their own time and their own money also. I actually think it's been a very good addition in the mandate that has been set out for companies. So, if you think about it in the Anglo-Western world we don't have enough research in India but if you look at research in the Anglo-Western world, I think the after the church, the biggest constituent of society is actually the corporations and therefore the expectations from corporations to give back, to help build a richer planet—for example, to remove some of the inequalities that exist especially in the case of a very stratified society—is actually going up and up and the expectations from corporations as you would know are becoming more and more complex. So, I think giving back and very frankly giving back is not just an altruistically good thing. I also find that I've actually seen this myself and have also read research as you would have to say that companies that do good are good corporate citizens actually get valued higher as well. So, from a very clinical point of view it makes sense just on the numbers part of it as well.

On climate change what is corporate India doing? Is it playing a leadership role in understanding the problem, to explaining to the less privileged that this is a serious problem? What does each one of us need to do, maybe simple thing like reducing carbon footprints. It sounds simple, not that simple but is corporate India taking a leadership role in this or should it be taking a leadership role?

Here, I think it's been mandated so we don't have a choice. What we need to do, what we have done is study more and more of technologies available. We're spending much more in terms of capex on CO2 emissions and other sustainability issues than we ever have in the past. In fact, I saw this year that we've actually cut back on some capex and allocated those funds to investing on sustainability initiatives. My only issue or my only contention is that, you have some areas which are mandated to have norms which don't exist anywhere in the world. So, I think we need to strike a balance. You can't tell me that your emission norm has to be 'X' when no one else in the world is able to meet that norm and worse still there doesn't exist a technology by which you can achieve 'X'. I mean, you can only achieve up to 'X' plus 20 percent. So, I think while it's a good initiative, whilst it has got us thinking, whilst it has got us spending in the right direction as any corporative of repute would do; I think that the mandate that is given in terms of the levels that are set need to become more realistic and also graded over a period of time. The expectations that you can adopt all of this in the course of one year or two years as compared to the several years that your Western counterparts have taken is I think, unrealistic and that's what needs to be looked into.

What about investor education? I know this is something that you have thought about that if the average investor is not educated, you will get very poor investment decisions by them and then they will blame the corporates for underperformance and then it builds increasing distrust and all of that. Do you find enough reach out to the average investor in terms of explaining where the company's head or is this annual forum that is available- the AGM is it that becoming a kind of a ritual without a worthwhile conversation with the shareholders that bother to turn up and the management? Is there a lot of shadow foxing?

I'm sure everyone who's been at an AGM know that not much that happens. There is poetry, there are flowers, sometimes abuse as well. Comments on quality of the pictures and the annual report. There is no qualitative discussion that happens. Investor education it has to be a continuous exercise. So, in our case we would have a small team of two people maybe in each company who only do investor relations the whole year round. So, investor relations are obviously a very important function that the corporate function division or normally a separate IR division needs to perform. I think it's becoming almost a run-of-the-mill that you need to have a certain number of non-deal road shows or whatever you might call them. We would actually compile which investors were met, by who, and the cause of the kind of discussions that were had, the concerns investors had and the manner in which they were addressed. So, I think that's become a very important role of management. Again, we are spending much more time on that than we've ever done in the past.

Audience Questions:

Ronojoy Dutta, CEO, InterGlobe Aviation: So recently, I read a report in the newspapers which said a large percentage of independent directors actually resigning from their posts because they were worried about the implied liability that they carry as independent directors. I was very perturbed by that. Do you have any comments to make on that?

Kumar Mangalam Birla: I agree. I think that, in many aspects, the role of independent directors is becoming way too onerous for someone at the end of end of the day isn't spending all of his or her time looking at the running of the company. But I think again, it's up to the company to give them comfort from the kind of disclosures that they make and the kind of comfort that they can give to independents about the governance standards that exist in the company. I think from what I understand is a balance that needs to be struck even in companies in the U.S., and in Europe that's a constant struggle. I think that more and more independent directors have to carry a more onerous role vis-à-vis minority shareholders for sure. M Damodaran: The good news is that a large number of offences under Company Law are going to be decriminalised. So, therefore you could get hit hard but you may not become a straight guest.

Mohandas Pai, Former CFO, Infosys: We have seen regulatory overreach in the last two or three years. Regulators pass laws which are overreach, and all these regulations could hurt good companies. They don't prevent the bad companies from changing. So what should they do to have a profit level of regulations?

M Damodaran: You said the last three years. If you would have said last 20 years, I would have winced but anyway, I didn't get a question.

Mohandas Pai: I'm saying there is regulatory overreach in industry today. There's too much of regulations coming, too much of criminalisation, somethings are being rolled back but they're not able to catch the bad guys who get away. But the problem is, for the good companies who follow norms, it creates such a big burden of fear, of not being able to follow this thing that you're going to miss something. What is the appropriate level of regulation? How should we handle this issue about regulators need to regulate and companies needing to be good citizens?

M Damodaran: No, maybe I'll take that question because whatever Mr. Birla may have done in his life he's not been a regulator. No, I think the answer is very simple. The laws are written for bad people not for good people. You can't have different sets of laws. So, as long as there are bad people, good people will pay the price. It's as simple as that because you got to write laws for bad people.

Kumar Mangalam Birla: I think the bigger issue also or another issue also is that of the multiplicity of regulators in a sector and having to provide the same information to different people or different people are asking the same thing from different perspectives or you can get caught out by one regulator not another. So it's a bit of being cat on a hot tin roof which I think is not a very desirable thing.