

## DO MANAGERMENTS SWEAT BOARD ENOUGH?

March 24, 2021

### SUMMARY OF DISCUSSIONS

#### Background

*The interaction between Boards and Managements is one of the major determinants of the performance of Boards. Each of them has to extract value from the other. Given that Boards have to provide superintendence, direction and control, the role of the Board vis-à-vis Management is reasonably clear. How well they execute it, is another story altogether.*

*The central question is whether Managements are able, and willing, to extract value from Boards. Do Managements see Boards as a value-neutral entity that they have to put up with? Or, do they see potential, and have to strive in order to extract value? Stated differently, do managements sweat their Boards enough?*

### DISCUSSIONS

- **Are managements sweating Boards?** - The answer is not a simple yes or no. But much more can be done. It depends on how much the management wants. The role of a Board is superintendence, direction and control. Most Boards do well in superintendence, and possibly in control. However, direction setting role of the Board is lacking.
- **Evolution of Boards** - Boards in India have moved away from being only ornamental. The Companies Act, 2013 has aided the move in the right direction. Boards are increasingly being valued for providing an outside in view.
- **Do Boards add value?** - Boards can be value destroying, value neutral or value adding. They however cannot be wished away. Many managements often wonder whether Boards are doing enough and adding value. And if they are not adding value, how can managements extract value from them?
- **Executive Directors (EDs)** - EDs often speak only when their subject is discussed in Board meetings. They tend to forget that too are Directors on the Board, and are expected to add value on all topics being discussed.
- **Relationship between Boards and managements** - Are Boards riding on the pillion of management? Are regulations forcing Boards to distrust managements? Board and management are not parties in opposition to each other. They have to work together, and have a joint responsibility towards the functioning of the company, including on matters such as compliance and strategy.
- **Expectations of stakeholders** - The expectations that regulators and stakeholders, including shareholders, have from Boards are very high. However, they should not lose sight of the fact that all Board members are not subject matter experts.
- **Alignment** - There should be an alignment between Board/management and shareholders, for the long-term success of the company.

- **Sweating is a two-way street?** - The Board should give comfort to the management that it is there to support and provide guidance to it, and not question all its decisions for the sake of asking questions. This may encourage managements to extract more value.
- **Possible causes for Boards not adding value** – Promoter of the company, or the management, may not be comfortable, and thereby be non-receptive to suggestions. There could also be a false perception that Board members cannot add value since they do not understand the business as well as promoters or management do.
- **Managements have to take the first step** – The starting point is for managements to want to extract value from their Boards. They should be open minded. The intention of the management is important. This is irrespective of whether the company is a promoter-led company or run by professionals. There is tremendous value that the Board can provide, and the management can derive.
- **Role of Chair** – As first among equals, a lot depends on him/her, irrespective of whether the Chair is executive or non-executive. He/she plays a vital role in creating the culture of trust, and that of the Board constructively challenging of the management. Also, he/she sets the tone at the top, wherein diversity of thought and expression is respected.
- **Board composition** - Decision to sweat the Board or not depends on whether the management wants a performing Board or a Board with marquee names. This call has to be taken by the management alone. It gets the Board it wants. Board composition is the starting point. If managements want their Boards to deliver, considerable thought and energy should be spent on selecting the right kind of Directors. Board members can also be chosen in a manner that they have prior experience which is complementary to the future plans of the company, since those Board members could guide management based on their own practical experience. This is particularly helpful if the company is planning to expand internationally or getting into M&A.
- **Diversity on Board** - Board composition should be looked at holistically. Diversity, skillsets, age, expertise, geographical spread, and international experience are all important. Skills/ Experience relating to AI and cyber are also becoming more important. Experience on other Boards is also important since the Director can use some of that experience for improving processes in the company. Boards should be diverse, but management should not lose sight of depth. Without diversity, there could be a risk of groupthink.
- **Experience versus Expertise on Board** - Experience and expertise are different, and a distinction should be made. Expertise can be brought by management, but experience comes from the Board. Collective wisdom that resides in the Board is richer than the individual experience of Directors.
- **Complementarities of Board members** - Managements need to consider both the experience of each Board member and the complementarities that they bring as a group. Many Board members are generalists, and not domain specialists. While setting expectations, this should not be lost sight of. Board members are not domain experts. To expect them to contribute on every issue can be counterproductive.

- **Refreshing Board composition** - As a company grows, and ground realities change, the context of a company also changes. Relevance of a Director, especially at the time of reappointment, should factor this in.
- **Induction of Board members** - Induction of Board members, and continuing upgradation of knowledge, can help Board members to contribute. This has to be initiated by the management, which has to ensure that the Board is immersed in the business of the company, so that its members can collectively contribute to the direction-setting for the company. It is also a great opportunity for the Board members and management to interact. This also enhances alignment.
- **Agenda of meetings** – Agenda of a meeting plays a very critical and important role. It should be structured in a manner that adequate time is given to each agenda item. It should be divided into discussion, debrief and decision items. There has to be clarity between the Board and the management on which item falls in which category, so that the focus is on discussions relating to items on strategy, risk, business prospects and the like.
- **Time commitment and duration of meetings** – Adequate time should be set apart for deliberations. Most Boards spend 20-30 hours annually in Board related deliberations (excluding committee commitments). This time has to be used by Board members to understand, discuss, deliberate and provide guidance to management, and therefore may not be adequate. Two-day Board meetings could be held, with one day focussing on compliance, and one exclusively for deliberations on business matters.
- **Too much focus on compliance** – The law leads to a focus on compliance. As per law, the responsibility of the Board should be towards strategy creation. But the focus of law seems to be on compliance, controls within the company and the role of Directors towards minority shareholders. Ideally, there should be reporting for exceptions on compliance matters. This is now possible with compliance softwares. In the interim, there could be a committee of the Board which could focus on compliance and routine matters.
- **Information flow** – Flow of information to the Board oscillates between very basic information and overload of information. Most Boards are prisoners of presentations. Also, they have to believe the information that comes to them, since there is no independent verification. A number of times, proposals contained in voluminous documents are approved without proper reading. There should be distillation done by management. At the same time, the Board should be updated on all vital information.
- **Board committees** – They play a very important role in functioning of the Board, and can be used to add value. In addition to the mandatory committees, there could be committees created specifically for some aspect of business or for specific issues. This would help with the committees focussing on, and deep-diving into, matters relating to their limited terms of reference. Further, more time allotted to lesser number of issues will help. If committees perform their role properly, and an ID chairs each committee, the Board can draw comfort from the functioning of the committees, and focus on strategy and related topics.
- **Focus on improvement** – Board processes and Board deliberations should focus on continuous improvement. Focus should be on futureproofing the company, and not to be looking at only of the

present. Sustainability of business should be the key area of focus. For this, enabling processes should be in place, and the Board should be objective in its discussions.

- **Continuing engagement between Board and management** – There should be engagement in between meetings too.
- **Exclusive strategy sessions** – These should be dedicated sessions for discussing strategy. These should last more than a day, and should ideally be twice a year. They should promote two-way communication between the Board and the management. There should also be discussions on how the company fares when compared with its peers.
- **Long-term strategic plans** - These have to be co-created by the Board and the management. These have to then be followed up with quarterly and annual reviews.
- **No agenda meetings** - There should be time set apart for only Board members to meet among themselves, and no specific agenda. Free flowing discussions, with no decisions to be taken, are useful. Management persons could be invited, if required, for specific items. Some companies also follow this practice for AC meetings.
- **Informal lunch or dinner** – These help break the ice between the Board members and the management, and are a good way to connect. There is apprehension on both sides. Board has some discomfort since it sometimes does not know what it is getting into.
- **Operations is an area for management** - A number of Board members are conscious of their role. They are aware that if they get involved in operational matters, their independence would get adversely impacted, and their role as Board members could be compromised.
- **Advisory Boards** - A number of companies have Advisory Boards, as distinct from Statutory Boards, with subject matter experts on them. Managements themselves are finding it difficult to keep pace with the ever-evolving world. Such Advisory Boards, with experts, can help managements on subject matters.
- **Mentoring** – The Board has a role in mentoring management personnel.
- **Management persons aligned to individual Board members** - In some companies, each member of executive management is aligned to a Board member, either on a rotational basis or on a continuing basis. This is to enhance communication on specific matters, beyond the boardroom. However, this would be successful only if the management person can extract value from the Board member.
- **Senior management** - Each company should focus on having a strong senior management team. These persons can add value in the informal engagements with Board members. They should also be encouraged to make presentations to the Board. Board should also ensure that enough processes are built into the company's functioning to ensure that the right people, with the right qualities, are at the right places. These processes should also be able to identify gaps, and/or training or upgradation requirements of senior management.

- **Group companies** - In group companies, expertise can be drawn from different companies or verticals. A number of times, senior persons from one company may be appointed to the Boards of other group companies. Such persons often play a balancing role among promoters, IDs and managements.
- **Feedback from Directors** – Management can seek feedback from the Board periodically. This is invaluable.
- **Compensation to Directors** – It should be reflective of their contribution in and between meetings. A similar amount of commission paid to all Directors does not do justice to those who have contributed more significantly than others.

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