BOARDS – EXPECTATIONS AND REALITY
JULY 9, 2024

SUMMARY OF DISCUSSIONS

Background

With stakeholders asking for better oversight, and with a regulatory overload that they have to cope with, Boards are seen to be falling short on delivering what is expected of them. Is there a mismatch between increasing expectations and the reality of Indian boardrooms?

DISCUSSIONS

- **Expectations from Boards** - The expectations of all stakeholders, including Regulators, shareholders and media, from Boards, are different and are very high. There might be a need to redesign, reinvent, or reengineer Boards, so that they add more value, and meet expectations. The Board has a role in protecting shareholder value, and for that it needs to know what will corrode value.

- **Involvement of Board** – The involvement of Boards varies, and it is the level of engagement of Board that decides its success. At the one end are passive Boards, and at the other are very involved Boards. There have been, and continue to be, Boards that are captured by managements. In such Boards, Directors usually are not engaged, with some of them being grateful to management for appointing them as Directors. There have also been Boards which have suffered from regulatory overreach. There too, involvement of Boards is constrained. Ideally, a well performing Board is one where the Board has autonomy, and the management is receptive to the ideas of the Board. Directors too should not be constrained by the presence of promoters, majority shareholders, Regulators or management.

- **Organisation and Board culture** – Contribution by a Board depends on the organisational culture. Board culture and organisational culture cannot be different. The Chair of the Board, whether promoter or non-promoter, plays an important role in driving culture. He/ She is responsible for setting the tone at the top. At the same time, the CEO too should be aligned. There have been occasions in the corporate world when a Board, as a collective, has found itself to be at variance with the organisational culture, and has not been able to add value. Transparency and trust have to be a part of the culture of any winning organisation.

- **Board composition** - Board composition plays a big role in determining the value addition that a Board will provide. Nomination and Remuneration Committees have to play a bigger and a more vital role. There is a need to constitute Boards with Directors who have the right competence and expertise, that is required on the Board. Independence of mind, in decision-making, is also very important while selecting and inducting Directors.

- **Board leadership** – The personality of the Chair of the Board plays an important role in deciding the conduct in the boardroom. It also impacts on the quality of discussions, engagement and decision-making in the Board. The Chair plays a huge role in ensuring that the management team moves in the right direction. Setting of the right tone at the top is very important. Participants in boardroom conversations should be encouraged to be outward looking, and focussing on improvement, rather than on finding faults.

- **Family run versus professionally run** – It is wrongly believed that the functioning of Boards, and their decision-making, depends on whether the company is family run or professionally managed. It is also erroneously believed that all family run businesses have an overhang of the promoter, while professionally run companies are run independently. The generalisation is wide off the mark.

- **Role of Board**– There is a lack of role clarity for Directors. The role of Board is superintendence, direction and control. It is expected to be involved in co-creating strategy. There is a need for having role clarity for Board and management. Board should balance the views of management and individual Directors. There can be a tendency for management to become overzealous, and it is for the Board to play a balancing role. The roles of Board and management should be clearly defined. Management should not hide behind the Board by getting transactions of a routine nature approved by them. Accountability of Board and management must be fixed based on their respective roles.

- **Role of Board in strategy** – Boards should co-pilot strategy, along with management. It is important for Boards to have strategy offsites. For these meetings to be productive, Directors and top management must have discussions, ideally without the aid of presentations, so that brainstorming can happen, and everyone's perspective can be considered. Some companies have moved to having two, instead of one, such annual meetings. These discussions should also consider competitor analysis. It is also important to analyse the progress a year later.

- **What is not the role of Board –** Board should not get involved in day-to-day functioning of the company. It should also be conscious of what it should not do. It is not the role of the Board to do backseat driving. This can especially happen if the Board has a domain expert or a former CEO as a Director. It is vital for the Board to trust the management. However, in some sectors, such as banking, the division in the role of Board and management is blurring, with Non-Executive Directors (NEDs) being held responsible for executive decisions.

- **Role of CEO** – It is important for the Board and the CEO to be aligned, and for each of them to understand the other's perspective. Prioritisation too is important. Most of the time, promoters/ Boards are receptive to ideas of the CEO. He/she should reach out to the Board members, as and when required, for their guidance. He/she should also encourage the top management to do so. Managements should not reach out to Board members only when there is a problem.

- **Board meetings** – The focus of Board meetings in most companies is only on statutory matters, with little to no discussions on vision, strategy, risks etc. This should change, and Directors too should be involved in suggesting agenda items.

- **Board Committees** - Board committees can play a bigger role in the proper functioning of the Board. Unfortunately, some committees of the Board, such as the Stakeholders Relationship Committee, play a very limited role in most companies. If needed, Boards can consider forming sub-committees to focus on any specific item that might require attention. This would take the burden off the Board, and the sub-committee can focus on the item.

- **Mentoring role of Board** – The Board members can play an important role in mentoring the CEO and top management of the company. However, very few Boards play this role at present.

- **Flow of information** – Often Boards do not get proper and timely information from management. For Boards to function properly, timeliness and quality of information, especially in the form of agenda documents, is important. It is equally important for the agenda to focus on giving information. Managements should not overload the Board with data which is not relevant. In some sectors, there is information overload on the Board because of the number of prescribed items. In such cases, the Board's time gets crowded out in approving items which are executive in nature, leaving little to no time for strategic discussions. It is also important for the agenda, complete in all respects, to be sent in advance, and for each Director to read the documents ahead of the meeting. The engagement has to be both by the Directors and the management. Providing timely, correct and complete information to the Directors is the starting point.

- **Updates between meetings** – Management should provide updates to the Board in between Board meetings. These could be in the form of monthly or important updates, and updates on regulatory changes. The management can also arrange for plant visits, if feasible, or sessions with consultants, so that the Board is aware of and abreast with the changes in the sector.

- **Independent Directors' (IDs) voice** – It is important for IDs to have a voice. Should an ID choose to resign, it should be for reasons mentioned in writing. All stakeholders deserve to know the true reasons behind the resignation. Regulators are taking note of comments being made by IDs in public domain, including in their resignation letters. There have been instances where if an ID has resigned for governance related reasons, the Regulator has initiated an enquiry against the company.

- **Board evaluation** – Processes such as a robust Board evaluation can add a lot of value to the functioning of Boards. Unfortunately, this is done mechanically, with performance of individual Directors not even being evaluated properly. Collegiality trumps independence.

- **Regulatory overreach** – Some Regulators have prescribed a large number of items that ought to be sent to the Board for consideration or decision-making. This has resulted in agenda documents being long, with some executive decisions also finding their way to the boardroom. There is also a tendency to inspect minutes of meetings for ascertaining individual contributions of Board members, and the duration of meetings. This has resulted in some companies writing transcripts, detailed with blow-by-blow account, in place of summary of discussions.

- **Interaction with auditors** – There should be increased engagement with Statutory Auditors and Internal Auditors. They provide a lot of important insights to Directors. With NFRA assuming a bigger role, and setting expectations from Audit Committees and Auditors, interactions with Auditors have become even more important.

- **Liabilities** – Regulators in India are becoming stricter, and the responsibility of Board members, especially IDs, is increasing. IDs have to become more engaged, to ensure that nothing important is missed by them. While considering the liability against a Director, it is important to consider the intent of the Director, whether or not he/she was familiar with the affairs of the company, and whether there was negligence on the part of the Director. Currently, there is an environment of fear that has been created.

While a number of Directors believe that Section 149(12) of the Companies Act, 2013 provides protection, the Section also needs a Director to prove that he/she acted diligently. It would depend on the Regulator to decide whether or not a Director had acted diligently. The burden of proof of innocence seems to have been pushed onto Directors.

- **Unlisted companies and Governance** – Unlisted companies, especially those above a certain size, should have proper Boards. Such companies often have the correct number of Directors on their Board. However, the Board does not perform its role properly. In unlisted companies too Boards have an important role, such as in considering the revenue recognition, projections and practices.

- **Startups and Governance** - For startups above a certain size, it is important to have proper functioning Boards. Nominee Directors of investors would often focus on numbers and growth, and it is for other members of the Board to focus on other aspects of the role of the Board. Among other things, Boards should play an important role in mentoring the promoter and top management. Unfortunately, governance is often seen as a cost, especially at the growth stage. It is important for promoters to understand that governance can add value, and the company is likely to get a premium if it has proper governance practices in place.

- **Boards abroad -** The fundamental difference between Indian Boards and global company Boards is that Indian Boards are statute driven. They spend more time on statutory issues. MNCs have a different Board culture. The management reaches out to Board members more often for advice or counselling.

- **Proxy advisory firms** - Quality of research done by such firms is questionable, and there have been some instances when their voting recommendations have not been uniform. They also have their own lens through which they tend to look at Board functioning. With increased reliance been placed on their recommendations, especially by institutions, Boards have reasons to be more careful.

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