


BOARD PERFORMANCE EVALUATIONS

A Journey from
'Good' to 'Great' Boards



INDEX

- 
- 01** Why is an effective Board Performance Evaluation imperative today?

 - 02** Board Evaluation trends across the world

 - 03** Why are Board Performance Assessments so critical?

 - 04** Answering the 3Ws

 - 05** What prevents boards from performing their best?

 - 06** IOD'S Approach to Board Performance Evaluation

 - 07** Key Takeaways

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In today's world, boards are in dire need of introspection. Changing geo-political landscapes, novel business compliances, transient regulatory frameworks, & additional expectations from stakeholders have constrained boards for self-assessment / board performance evaluation that not only check for inefficiencies but more importantly, provide bias-free implementable solutions for inclusive growth.

Major global economies including France and the United Kingdom recommend 'Third-Party Performance Evaluations'. It is crucial to know what board evaluations entail, the risks of not undergoing board evaluations and associated global trends.



1

Why is an Effective Board Performance Evaluation Imperative Today?

“ What gets measured, gets managed

- *Peter Drucker, Austrian-America Management Thinker, Professor, and Author*

- **Appraising Board Performance**

Many companies attribute their success to an effective board of directors. Board assessments facilitated by external agencies provides an unbiased view of board's effectiveness. Companies across the world are voluntarily opting for third-party board assessments, solely to enhance their organisational performance. It aids in foregoing inefficient board practises, while identifying and adopting a fresh growth-oriented culture.

- **Changing Investor Expectations**

There are very visible new trends in investor expectations from boards. There is rising need for transparency, in not just remunerations and fee, but also processes and behaviours of the boards. Investors are setting higher standards and want to invest with purpose i.e. they're becoming more and more interested in non-financial investing factors such as 'socially-responsible investing'. They are examining both operational strengths and potential threats caused by board shortcomings. Investors are looking across dimensions such as fee, relationships, risk/return, operational strength, the macroeconomic and political environment, and ESG compliance. Additionally, social media has now provided them with a forum to voice their opinions, including their displeasure with businesses that fall short of their expectations. **This means that boards need to be on their toes, now more than ever.** On account of the growing oversight responsibilities and accountability of boards triggered by these transforming investor expectations, boards have taken on a distinct level of complexity.

In this environment, boards must monitor their own performance as well as that of management. Boards must undertake '**Board Performance Evaluations**' to examine where they stand and find the most effective approach to maintain a culture of high performance in the boardroom while meeting business and investor objectives.



Regular performance evaluations shelter companies from corporate failures and are the only proven effective way to prevent company collapse.

2

Why is an Effective Board Performance Evaluation Imperative Today?

Regulatory Requirement for Board Evaluation in India

It is a regulatory requirement to conduct Board Evaluations in India. The regulatory standards pertaining to Board Performance Evaluation in India are substantially consistent with those in the United States.

- The Companies Act, 2013 requires listed companies to report the yearly evaluation procedure for the board, its committees, and its individual directors.
- The SEBI Listing Obligations and Disclosure Requirements (LODR) Regulations, 2015 require that the performance of the board's individual directors, including the independent directors and chairman, as well as the board's several committees, be evaluated.

Even though board assessments in India are still in their buoyant stage, mandated laws and regulations have resulted in a number of developments in the review and disclosure practises of listed companies in India.

Board Evaluation Trends in Other Countries

Globally, the stance on board evaluation is not uniform and is quite varied. The below table outlines the different approaches:

Countries with Board Evaluation Rules and Regulations	India, Spain and United States
Countries with Board Evaluation Principles in their Corporate Governance Codes	Japan, Singapore, South Africa, Brazil, Switzerland, Germany, Austria, Hungary, The Netherlands, France, Italy, Luxembourg and United Kingdom
Countries with Implicit Board Evaluation Requirements	Poland and Turkey
Countries with Emerging Board Evaluation Practices	Israel
China is the only country without any Board Evaluation Regulation	

Source: Board Evaluation: Overview of International Practices © OECD 2018

“ Following the sale of Nokia to Microsoft in 2013, the CEO of Nokia, at the last press conference, said, “We didn't do anything wrong, but somehow we lost.”

3

Why are Board Performance Assessments so critical?

1. **CimplyFive** as part of its fourth report of the 'Board Evaluation Report' series surveyed nifty-50 companies based on disclosures made in their annual reports. The report highlighted:
 - that even though board performance assessments are not mandated by law in India, 24% of the companies engage external consultants for facilitating their corporate board evaluation process.
 - 18% of the companies using an online digital survey tool to ensure anonymity of response for a **free and fair evaluation process** by eliciting constructive feedback.
2. It is pertinent to note that PSUs are not legally required to conduct board evaluations, but research shows that many PSU's have been conducting board evaluations to improve performance and decision making.

According to a research conducted by the **National Stock Exchange of India Limited (NSE)** in partnership with the **Institutional Investor Advisory Services (IIAS)** in 2019-20 where they surveyed 100 companies including PSUs, the below was the result:

Evaluation of:	Number of companies that conducted evaluations (Out of 100 surveyed Companies)	
	2017	2020
Entire Board	86	88
Board Committees	82	84
Individual Directors	85	89
Chairpersons	63	78

The research reflected that there is a swiftly rising trend in board performance evaluations in companies. Individual directors & entire boards collectively were being evaluated by the maximum number of companies. The above research shows that evaluations are being conducted now more than ever, not just because it is a legal requirement for listed companies, but also because these evaluation practises have tangibly helped in improving board performance.

As a result, in 2017, SEBI issued a '**Guidance Note on Board Evaluation**' with the aim of apprising listed companies and their boards about the detailed evaluation process and educating all relevant players about board performance procedures.

3. **UK Spencer Stuart Board Index** is a comprehensive review of board composition and governance practice in the largest 150 companies in the FTSE rankings, providing a valuable perspective on the health of boardrooms during 2021–2022. Below is an International Comparison Chart on Spencer Stuart Index of Board Metrics across 25 Countries for the year 2022.

Country	Board Meetings/Year	% Boards With An External Evaluation	Avg. Board Size (Total)	% Independent Board Members
Belgium	9	19%	10	49%
Canada	10	--	11	81%
Chile	--	--	8	20%
Denmark	13	36%	10	77%
Finland	14	16%	9	88%
France	9	60%	14	69%
Hong Kong	7	3%	11	43%
Ireland	11	20%	10	71%
Italy	13	40%	11	58%
Netherlands	9	14%	7	84%
Norway	13	20%	8	73%
Singapore	6	17%	10	61%
Spain	11	37%	11	47%
Sweden	13	20%	11	69%
Switzerland	8	4%	11	90%
Turkey	19	n/a	10	33%
UK	8	42%	10	73%
USA	8	25%	11	86%

The chart below provides a unique perspective on the extent to which a range of key metrics have changed over the past five and ten years for largest 150 companies in the FTSE rankings by market value at April 30, 2022.

Meetings and Board Evaluation	2022	2022	2022	5yr change	10yr change
% boards external evaluation	77%	39%	43%	98.8%	80.5%
Average number of board meetings (scheduled)	8.0%	8.8%	8%	-9.0%	0.1%

The current **UK Corporate Governance Code** recommends that an external independent board evaluation should be conducted every three years. 95% of companies disclosed that they conducted an annual board evaluation during the period under review. 49% of them ran an externally facilitated review, up from last year's 44%.

4

Answering the 3Ws

When should a board be evaluated?

Most commonly, boards across the world conduct evaluations on an annual basis during the last quarter of the fiscal year.

More so, board evaluations must also be undertaken in response to changing company operations. For instance, if a company is undergoing a merger, or if a company is expanding to an international space, or if a company has had a disappointing stock price performance, then in all these circumstances, board evaluations will become a necessary tool to be able to adapt to the transient market.

What should be evaluated?

Effective board evaluations are holistic in nature encompassing multiple areas that include:

Board Structure & Composition	Board Committees	Company Strategy	Board Dynamics	Compliance
<ul style="list-style-type: none">• Size of the board• Diversity of the board• Qualifications of Board Members• Practical Skills• Industry Experience• Soft Skills	<ul style="list-style-type: none">• Structure• Functioning• Effectiveness	<ul style="list-style-type: none">• Quality of the monitoring and risk-management role• Quality of the strategic and other business-related advice• Degree of shareholder engagement• Degree of stakeholder management• Oversight of management performance, compensation & succession planning	<ul style="list-style-type: none">• Board members' pro-active participation• Board practices• Board decorum• Efficiency• Frequency of Board Meetings• Minority Interests	<ul style="list-style-type: none">• Board's compliance with its legal, regulatory & fiduciary responsibilities• Corporate Governance framework

Who conducts these evaluations?

Most guidelines and codes across the world prescribe board evaluation to be conducted either internally or externally. It is considered ideal for the NRC Committee, board chair or independent directors to conduct internal evaluations. However, as the functions and responsibilities of the board chair, NRC committee and independent directors are part of the performance review; their impartiality becomes a matter of conflict.

Solution: External institutions conducting board evaluations are becoming a more popular trend and productive option, particularly for organisations seeking an independent and unbiased evaluation. The [Board Research & Advisory Department](#) of Institute of Directors, India is one such agency.

5

What prevents boards from performing their best?

Why Internal Evaluation of Boards may not arrive at the Right Conclusions

The main causes of dysfunction in boardrooms typically stem from interpersonal dynamics and board culture. Disruptive or disengaged directors, divisions in the boardroom, a lack of trust between the board and CEO, or inadequate decision-making procedures are just a few examples of how dysfunction can manifest. Even though these problems are sometimes obvious to people in the boardroom, they might be the most challenging to resolve. This is where performance evaluations come into use.

However, performance evaluations take time, and sensitive issues usually encumber the process. Boards need to invest substantial time and effort to make these exercises valuable to their organisations. These initiatives need a high level of dedication and direction from the chairperson. Boards would need to get familiar with the concept as well as the methods and techniques to be employed, even if they had not previously practised them or have had reservations around them.



Effective performance is preceded by a lot of painstaking preparation.

- Brain Tracy



- Boards need to carefully curate and draft self-assessment tools such as, questionnaires, assessment forms, interview questions and so forth.
- Boards need to ensure that evaluations are conducted in the presence of experienced and senior evaluators, to be able to lead independent, effective, & a good-mannered assessment.
- Boards must ensure that evaluation results must not be inadvertently exposed in any way whatsoever. Board weaknesses, if not attended to, may become reasons for litigation later.
- Evaluation results should remain confidential. Results should be distributed to board members, and be deliberated upon in an open and non-confrontational manner.
- Boards must realize that evaluations can be a sensitive issue to some people, hence it is important to be aware of this possibility and to deal with sensitivities in the right manner.
- Peer-evaluation may deteriorate board collegiality. Hence, special attention is required to handle director's comments on peers, and unanimous effort of the board is required to ensure that comments and answers are not too harsh or ill-considered.
- At the same time, boards need to take care that the evaluation process is not just a formal exercise conducted in vain, but should tangibly help in improving the board performance.
- Safeguards should be built into the system to protect both the company and individual directors.
- Careful consideration should take place before management is included in the evaluation process. The presence of management may constrain directors' comments.
- There is high possibility that boards repeat the same self-assessment methods each year, up until there is deterioration in the effectiveness of evaluation tools itself. Hence, self-assessment tools must be updated and changed to prolong its effectiveness.
- Boards need to avoid **corporate hubris**, collectively as well as individually, as it can seriously impede with the self-assessment of performance. Corporate hubris is a major adversary of corporate sustainability.

External assessments help a long way in sidestepping the issue of corporate hubris.



6

IOD's Approach to Board Performance Evaluation

At the Institute of Directors, India (IOD) we understand the dynamics of boardrooms, how the idea of questioning a fellow director's performance cannot be welcoming. IOD goes beyond this traditional outlook, and has brought in a 'Constructive Approach' to board performance evaluations and also provide the directors with training opportunities. We have custom-tailored solutions for each client, as 'one size does not fit all'.

Even though receiving feedback from a board review might be daunting, high-performing boards today are required to periodically assess their own performance and that of their procedures in order to make improvements.

Getting the most from your Board Evaluation

Our take on Board Performance Evaluations takes into consideration the following:

1. Providing constructive evaluation results, keeping in mind the 'vision & mission' of the company and aligning the company towards it.
2. Reflecting a mirror image of how the board, as a whole, perceives where the company stands, with respect to its Key Performance Indicators (KPIs).
3. Analysing and understanding the perception of committee members on the board committee's effectiveness and functioning.
4. Conducting performance evaluation of the board chair, each individual director, and board committees keeping in mind the industry, sector and type of company.
5. Developing concrete and implementable insights as part of the evaluation results, to further aid in organizing the business and maintain the collegiality of the board and its committees.
6. Identifying training needs of directors.
7. Seeking special inputs from both governance & industry experts.



NOT the standard 'Tick the Box' approach at IOD

IOD follows a **Three-Tier Approach** to have a complete understanding of the Boardrooms.

TIER I: Quantitative Questionnaires (customized to industry requirement)

TIER II: Qualitative Questionnaires aligned with company's industry and outlook

TIER III: One-on-One interactions amongst Board members and IOD Board Experts (Governance & Industry specialist)

Additional information is sorted via:

- Attending board and/or committee meetings as silent observer
- Document analysis including meeting minutes, annual report, policies and guidelines

Advantage of External Board Performance Evaluations

- Helps understand how to better utilise the skills of the directors;
- How to help the board better serve the organisation;
- Identify areas of high risk and emerging risks, &
- The need for any new strategic changes

Culture of Trust: Keeping it Confidential

The obligation of confidentiality fundamentally derives from fiduciary duties of loyalty and care. IOD fosters a culture of trust as a matter of best practice and is really a strong proponent of the same. We understand that unauthorised disclosures of sensitive information may endanger a company's capacity to remain competitive or to achieve financial success, and therefore IOD, India conducts these assessments which are completely protected by a Confidentiality & Non-Disclosure Agreement.



7

Key Takeaways

- On account of the growing oversight responsibilities and accountability of boards triggered by transforming investor expectations, boards have taken on a distinct level of complexity.
- Regular performance evaluations shelter companies from corporate failures and are considered effective way to prevent company collapse.
- Board performance evaluations have become an international good corporate practise, irrespective of legal requirements. However, it is **mandatory** for listed companies in India to conduct board performance evaluations vide clause 49 of the Listing Agreement applicable to listed companies. Further, Section 134, 149 and 178 of the Companies Act, 2013 provides the provisions for board performance evaluation.
- Board evaluations need to be responsive to changing company operations. Boards need to invest substantial time and effort to make these exercises valuable to their organisations. Depending on skills, resources and time, companies can opt for external board performance evaluations from independent professional experts.
- Using a '**Constructive Approach**', IOD provides '**tailored**' actionable insights as part of Board performance evaluations for each company, as 'one size does not fit all'.



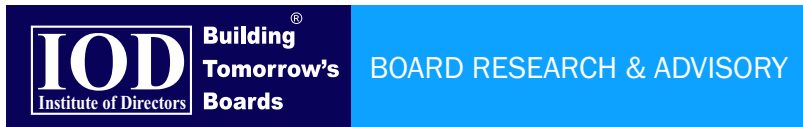
Great governance is a journey, not a destination. Past performance is no guarantee of future success. A board that becomes self-satisfied is a board that will underperform its full potential. So it is imperative to develop a culture of self-growth within the board.

We know it takes a strong leader to change a board's culture.

Are YOU that strong leader?

Contact us at:

info@iodglobal.com



The Board Research & Advisory department at Institute of Directors, India provides the following **Governance-related** services:

- Annual Board & Directors' Performance Evaluation
- Governance Review
- Performance Evaluation of Public Interest Directors (mandated by SEBI)
- Performance Evaluation of Independent External Persons (mandated by SEBI)
- Board Skills Evaluation
- KMP Evaluation
- ESG Advisory

To know more about our services and Board Experts Panel, visit <https://www.iodglobal.com/advisory>

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