

On the 2020 nomination committee agenda

Board Leadership Centre



The nomination committee agenda for 2020 needs to be sharp, focused, and executed with resolve. The nomination committee is operating in a business environment shaped by coronavirus crisis, technological and digital innovation, cybersecurity risks, and scrutiny of corporate culture, as well as growing demands to address environmental and social issues and activism by shareholders, employees, and other stakeholders – all against a backdrop of geopolitical volatility and economic uncertainty. The demands on boards have never been greater, and in the year ahead, the nomination committee will be under intense pressure to help the chairman with excellence by optimising the board's composition, structure and operations.

Drawing on insights from our work and interactions with nomination committee members, board chairs, company secretaries and business leaders, we highlight seven items for nomination committees to keep in mind as they consider and carry out their 2020 agendas:

- Aligning talent to strategy and developing succession plans for committee members and the chairman
- Enriching through diversity
- Refocusing on the committee's remit
- Conduct rigorous assessments to drive continuous improvement in board and individual director performance
- Challenging conventional wisdom
- Increasing transparency for investors
- Update the approach to new-director onboarding and continuing director education

Aligning talent to strategy and developing succession plans for the board and management

The item at the top of nomination committee agenda continues to be pipeline management and how best to align boardroom talent with corporate strategy, both for the short and long-term – whether it's addressing a gap around technology or finding people who have

international experience, talent needs to be part of the strategy discussion.

Boardroom composition and succession starts with clarity over the company strategy – identifying the business requirements and how they need to develop over time allows for a detailed examination of the skills required to deliver on them. Use skills matrices to identify current and future skills gaps and remember to factor the opportunities for ongoing professional development when developing long term succession plans.

Chairman should be agile and quick to adapt to help their companies meet the challenges of the future and they need to be capable of catalysing and orchestrating a transformation in how the board is composed and structured, how it operates and interacts with business, and how it holds itself accountable.

Nomination committees need to look ahead in order to understand when individuals are due to (or likely to) leave the board. Scenarios where a number of directors are planning to leave at the same time, or are required to rotate off the board, need handling carefully both in terms of disruption and corporate memory, but also in terms of managing investor expectations.

When considering CEO succession, be wary of looking to clone the current CEO. The company may have changed since they were appointed and different characteristics may be more crucial to the future success. Ensure a comprehensive review is undertaken by the committee of the role description and skills requirements.

Through modelling personal integrity, demonstrating independence of thought, and encouraging dissenting viewpoints – as well as collaboration and reaching consensus – chairman should set the tone for the board's overall culture. Board chairman, in particular, must be a strategic thinker, always keeping the big picture in view, as well as being perceived as trusted, discrete, independent and objective.

Enriching through diversity

Core to the responsibilities of the nomination committee is ensuring that their board has the right combination of skills, backgrounds, experiences, and perspectives – to probe management's strategic assumptions; to enable management to navigate the company through an increasingly volatile and fast-paced global environment – and diversity is one of the most penetrative tools for achieving this.

Diversity is about the richness of the board as a whole, and the combined contribution of a group of people with different skills and perspectives – people with different experiences, backgrounds and life-styles who together are more able to consider issues in a rounded, holistic way and offer an attention to detail that might not be present on less diverse boards.

Diversity can be measured in so many ways – from race, sexual orientation and disability, to geographical heritage. International diversity is especially important for businesses operating across many different markets.

“ *Board diversity promotes effective decision-making and enhances corporate governance. The consideration of diversity is becoming an increasingly important factor when investors make their investment decisions. Promotion of board diversity is a key focus of the Exchange and an area we are committed to continuing to develop.* **”**

Mr. Graham, Head of Listing, 2019.

Expectations for board diversity (including gender) continue to move from interest to action – a new listing rule by HKEX requires boards of companies to have a policy on diversity and to disclose the policy or a summary of the policy in the company's corporate governance report effective January 2019 1.

A diverse board will, by definition, have a number of diverse personalities and getting the most out of them is what sets great chair persons apart: a chair who understands the differences between board members and how they approach any given situation will be better placed to harness their skills and attributes and ensure that the board as a whole is greater than the sum of its parts. Psychometric profiling can be a useful tool in assessing the emotional intelligence of existing and incoming board members.

Think about the breadth of the talent pool from which new board members are sought. Has sufficient attention has been given to recruiting directors with backgrounds in the third sector, academia and government, as well as entrepreneurs and those from family businesses?

Nomination committees should challenge recruitment firms to provide a more diverse list of candidates and be specific about the skills and attributes required. Nomination committees that are themselves diverse, are likely to be more open to bringing in others from more diverse backgrounds.

Refocusing on the committee's remit

Do the nomination committee terms of reference reflect the actual role carried out by the committee? Is the committee's role restricted to leading the process for board appointments or does it extend as far as executive and senior employee succession and talent management? Managing the balance can be difficult. While the nomination committee is required to ensure that plans for succession to both board and senior management positions are in place, it is management's responsibility to prepare and deliver on them.

The committee must ensure that there is adequate 'bench strength' within executive management while remaining cautious not to breach the line between oversight and management as CEOs will, quite naturally, expect to take responsibility for appointing their own teams.

As well as the traditional role of board appointments and pipeline, nomination committees may want to be considering their role with regard to the annual board evaluation, induction training and continuous development, as well as any wider remit for other governance matters.

Conduct rigorous assessments to drive continuous improvement in board and individual director performance

In Hong Kong, board assessment remains a recommended best practice, and whilst informal reviews of board performance are common, relatively few companies have set up a regular and formal evaluation process, much less one which involves the use of external parties². Compared to other countries such as the U.K. where board assessment has been a mandatory requirement, Hong Kong is still lagging behind in uplifting the governance standard.

If the board has not already defined its expectations for individual directors, this is a good place for the nomination committee to start, by creating a detailed director role description outlining responsibilities, performance standards, and expectations inside and outside the boardroom. Expectations should be clear not only as to

preparation for and attendance at meetings but also that each director must become a student of the company and its strategy. While it's management's role to educate the board about the competitive environment and the implications for strategy, directors need to take control of their own education – reading, visiting facilities, and experiencing the business firsthand – to make sure they understand the strategy and its risks. Reaching a collective understanding of what the board expects from its members can help set the tone for a high-performing board and form the basis for individual director evaluation and action in the future.

As a matter of best practice, board, committee, and individual director evaluations should periodically be undertaken by an independent third party who conducts one-on-one interviews with directors and senior executives and provides benchmarking against peers. Some boards find it helpful to take a deep dive on a particular area – e.g., CEO succession, oversight of disruptive risk, or oversight of talent development – in addition to the standard board assessment. And, of course, follow-through – particularly if removal of an underperforming director is called for – is critical and a test of board leadership.

Challenging conventional wisdom

Rapid technological change and new disruptive business models challenge the more traditional approaches of many established businesses. Companies need to consider the impact of this on their board and look at a wider pool of candidates in order to identify people with the skills needed for them to meet the challenges they face in this new environment.

Traditionally, boards sought out directors with 'big company' experience, but in this new age the ability to understand and leverage technology at speed are vital to success and so a different sort of experience is needed. Nomination committees who don't evolve risk creating boards which are found lacking in the most valuable executive currencies of youth and IT literacy.

Individuals with deep technological expertise can be hired at an executive level but board members still need to be able to 'ask the right questions' and just as important, 'understand the answers', in order to be capable of contributing across the range of issues the board faces – but have the risks around inexperience been historically overstated? And even if not, have they now been surpassed by the potentially higher risks associated with a board lacking in technology literacy?

Consider looking beyond the 'usual suspects' to find people with different experiences and backgrounds – including those who have not served on a listed company board before. With appropriate induction, mentoring and coaching, new directors should be able to adapt reasonably quickly.

Alternatively, consider the use of an advisory body – composed of independent individuals with expertise in specific fields – to advise the board on areas such as technology and innovation. Being less onerous in terms of time commitment and legal responsibilities, such roles might be more attractive to younger less experienced individuals.



Increasing transparency for investors

Investors are increasingly interested in succession planning arrangements and how boards assess both director and management performance, yet it can be argued that many nomination committee reports lack the rigour and attention to detail associated with both audit committee and remuneration committee reports.

To achieve a higher level of corporate governance, HKEX published the conclusion of its consultation on Corporate Governance Code ("the CG Code") in July 2018. New measures were introduced to strengthen the accountability of the board and the nomination committee, improve transparency of independent non-executive directors' ("INEDs") relationships with issuers, and enhance the independence criteria for assessing potential INED candidates.³

The consultation conclusion strengthened disclosure requirements including the process of identification and considerations of INED's perspective, skills and experience that INED may bring to the board to submit in accordance with the resolution to elect the INED. Other key changes include requiring board or nomination committee to assess the time commitment of the INED candidate to the issuer and the independence of the INED candidate based on the list of factors (e.g. any material interests in issuer's principal business activities) defined by HKEX. With more stringent disclosure requirements, is the nomination committee clear on the company's regulatory responsibilities?

To demonstrate the board's commitment to sound governance, the committee should see that the disclosure statement serves as a communication tool as well as a legally mandated document. Consider including a letter from the full board or chairman, a section with governance highlights that includes a description of the board's evaluation and improvement initiatives, and a board composition matrix showcasing the board's diversity and linkage between director skill sets and company strategy and risk. Recognise that the business implications of climate change are high on the priority lists of most investors, and consider whether the company's disclosures on this issue should be enhanced. Also make sure to stay current on the topics that are likely to be top of mind for investors in 2020, including director overboarding concerns, director pay, and corporate structural issues.

Update the approach to new-director onboarding and continuing director education.

The complexity of the business and risk environment and the speed of change today throws new directors into strategic conversations on day one, making the onboarding process particularly important and challenging. Keeping in mind the director's background, the company's key issues, and the role(s) the new director will fill on the board or committees, what are the most important areas for the new director to know about up front? Highlight these areas and work with management to shape a tailored program. The new director should also play an active role in onboarding, requesting meetings or materials as needed.

Onboarding should be an ongoing process rather than a once-and-done event. New directors may be paired with a board mentor which can be helpful to fill information gaps and to provide an opportunity to ask questions about the company based on a more nuanced understanding of the company's strategy and operations.

Directors should be expected to participate in continuing education, and the nomination committee should consider how to enable collaboration and coordination to maximise value. For example, the committee may suggest key areas for board education, identify top-tier programs covering each topic, and establish a process by which individual directors (or small groups) each cover different topics, followed by a debrief to the full board. The board or committee may also choose to attend a board governance or industry conference together, followed by a robust discussion with management about the implications for the company.

¹ HKEX, [Guidance for Boards and Directors](#) (2018)

² The Hong Kong Institute of Chartered Secretaries, [Board Evaluation Best Practice Update](#) (2019)

³ HKEX, [Exchange Publishes CG Code Consultation Conclusions and Guidance for Boards and Directors](#) (2018)

KPMG Board Leadership Centre

The KPMG Board Leadership Centre offers support and guidance to non-executive directors, whether managing a portfolio non-executive career or embarking on a first appointment. Membership offers you a place within a community of board-level peers with access to topical and relevant seminars, invaluable resources and thought leadership, as well as lively and engaging networking opportunities. We equip you with the tools you need to be highly effective in your role, enabling you to focus on the issues that really matter to you and your business.

Learn more at kpmg.com/cn/boardleadership.

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