On the nomination and remuneration committee agenda 2023

Board Leadership Center (India)

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With various countries around the globe facing an imminent recession, many businesses in India continue to make hard choices to prepare themselves for any potential volatile conditions. While some businesses have optimised investment in workforce and made businesses more sustainable, business recovery, growth, Environmental, Social and Governance (ESG) commitments and the long-term effects of the pandemic continue to test the robustness of governance practices and the skills and experience of its board members. How is the NRC preparing the board to support new strategies, review executive succession, and create a conducive environment for fairness, equality and opportunity allowing talented people to succeed? We highlight seven pertinent issues for the nomination and remuneration committees (NRC) in India to keep in mind as they consider and carry out their 2023 agendas.

Skillset to expand and enhance ESG oversight

ESG has gained significant momentum for businesses, investors and shareholders across all sectors. In recent years, investors and stakeholders have placed increasing importance on ESG considerations, and boards must have the appropriate skillset to effectively manage and enhance their oversight of ESG issues. Climate change continues to be in the forefront and social factors have gained greater attention over the past year. The pandemic not only affected the working and living practices but also the cost-of-living that highlights existing social issues.

Risks, such as climate change, supply chain disruptions, and social issues, have a significant impact on an organisation's operations and financial performance. These risks need to be acknowledged and managed so that organisations can safeguard their reputation and financial stability. Investors are increasingly incorporating ESG considerations into their investment decisions. Companies that demonstrate strong ESG performance are more likely to attract investment and access to capital. Governments and regulators are increasingly mandating ESG reporting and disclosure requirements. Consumers and stakeholders increasingly expect businesses to act responsibly. An organisation that has a strong reputation for responsible business practices attracts more customers and stakeholders, leading to increased profits and growth.

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Oversight of ESG related risks – and equally importantly, the opportunities – starts with an ESG competent board. Not every board member needs to have deep-dive ESG expertise, but the board needs to have ESG risk and its impact on long-term value creation, top of mind. The board needs to understand which issues are of greatest risk or strategic significance to the company, how they are embedded into the company's core business activities, and whether there is strong executive leadership behind the company's response to the climate crisis.

Oversight of these risks and opportunities is a significant challenge, involving the full board and potentially multiple board committees.

Board members need to have a comprehensive understanding of ESG issues, including the potential risks and opportunities associated with these factors. By having a thorough understanding of ESG considerations, boards can make informed decisions that positively impact the company's financial and social performance. Board's skillset is thus essential in expanding and enhancing ESG oversight. By having the appropriate skills and expertise, boards can effectively manage ESG risks, engage stakeholders, and develop sustainable strategies that positively impact the company's financial and social performance.

Questions to consider:

- How is the NRC ensuring that the board has the right skills and governance structures?
- Is this addressed as part of the annual board evaluation exercise?
- Is ESG explicitly addressed in company's succession plans?

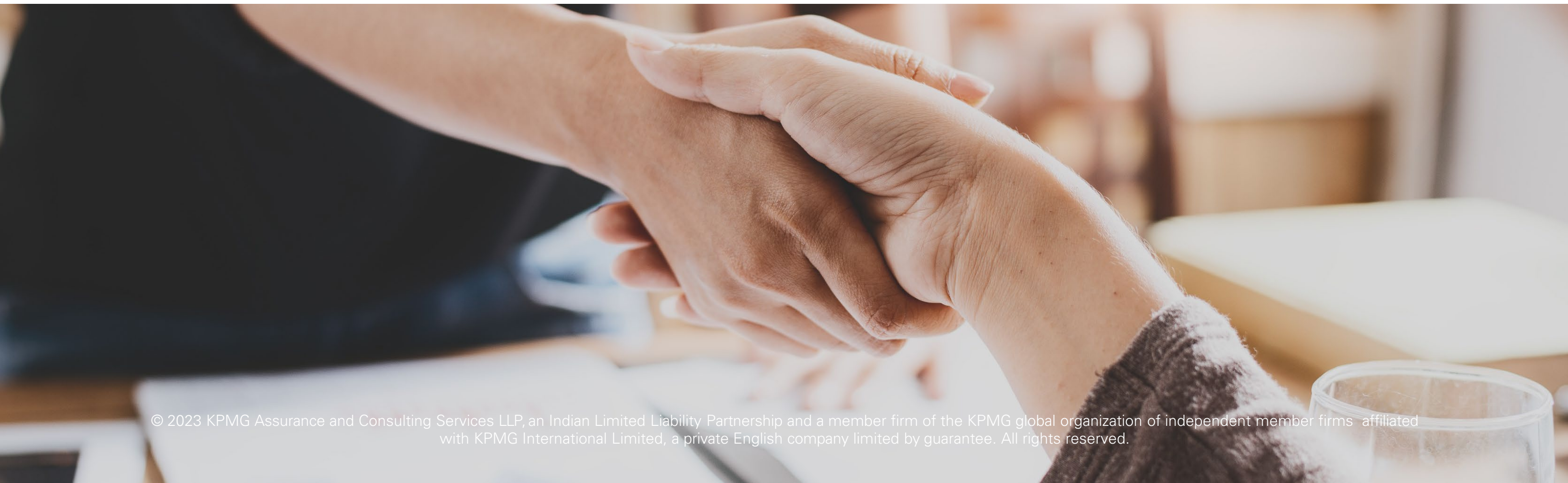
Evolving trends in executive recruitment and selection

Core to the NRC's role is ensuring that the board has the right combination of skills, backgrounds, experiences, and perspectives to probe and challenge management's strategic assumptions and to support management in navigating the company through an increasingly volatile and fast-paced global environment.

Companies are placing a greater emphasis on diversity in their boardrooms, with a particular focus on gender, and skills. This is driven by a recognition of the benefits of diverse perspectives and experiences, as well as changing social attitudes and legal requirements. Technology is emerging with an increasing role in board executive recruitment and selection. Online job boards, social media platforms, and applicant tracking systems are all being used to attract and assess candidates. Companies are also increasingly involving a wider range of stakeholders in board executive recruitment and selection. Unlike a few western economies, organisations in India are not yet looking to adopt more rigorous assessment processes to evaluate candidates which includes the use of psychometric testing, competency-based interviews, and assessment centres.

Questions to consider:

- Does the NRC use appropriate testing methodologies or cognitive profiling to evaluate the right mix of personalities and decision-making styles that best contribute to effective oversight and decision making?
- Considering the breadth of the talent pool from which new board members are sought, has sufficient attention been given to hiring directors with experience in different sectors, academia and government, as well as entrepreneurs and those from family businesses?



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Board capability development

Talent is a critical priority for CEOs over the next three years alongside advancing digitisation and adapting to geopolitical issues. While the pandemic may have highlighted key skillset required to deal with the crisis, the continuing priority is to ensure that talent in the boardroom and in the pipeline, is retained and aligned to strategy – be clear on what the company's strategy is, and where the skills gaps are in relation to that strategy.

There continues to be a great demand for experience in business transformation, recovery, technology and restructuring. Leadership styles have moved more towards empathetic leadership and wellbeing, including a greater focus on women's health and continued inclusion in the workforce, remain high on the agenda.

Advisory boards might be considered as an effective mechanism to fill skill gaps and support the board in the execution of its duties.

However, clarity over their role, authority and place within the organisation's governance framework will be critical for success.

Equally, the use of external advisors to support the board in areas where specific expertise is required is likely to continue, but regulators and investors are increasingly seeking greater transparency around who such advisors are and any affiliations, financial interests or ties that might bias their judgement and therefore impact their advice.

Maturity in areas of digitalisation, robotics and AI is now an increasingly important component of many corporate strategies. 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'.

It is desirable to find individuals with specific skills who are also capable of contributing across the range of issues the board faces – not least because the board as a whole is responsible for all decisions, regardless of the expertise or knowledge of an individual director in that area – but have the risks around inexperience been 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. Different leadership styles may unlock organisational success, and with appropriate induction, mentoring and coaching, new directors should be able to adapt reasonably quickly.

Courage, integrity and the emotional intelligence to provide a balance of perspectives should not be underestimated as key requirements to help the CEO and organisation recover and support growth once again.

Questions to consider:

- ? What steps is the NRC taking to ensure the board, leadership and senior management team are well suited and well placed to support business recovery and growth?
- ? Apart from desirable skillset, is NRC looking to onboard directors with technology literacy?
- ? What development plans are in place to facilitate senior managers and their future successors?

Managing pay disparity in organisations

Pay disparity, whether related to diversity or nature of roles/level, has been a critical factor that has differentiated majority of organisations from the best on how meticulously they are evaluating and addressing these discrepancies. Multiple global and India studies have consistently highlighted this disparity between levels and how this pay disparity is detached at times from the inflation levels in the economy.

Addressing pay disparities can help organisations retain their employees and attract new talent. When employees feel that they are being paid fairly, they are more likely to be engaged with the organisation and recommend it to others. The role of the NRC is critical in ensuring important decisions related to pay harmonisation are done effectively in a time bound manner to drive inclusion, productivity and performance.

Questions to consider:

- ? How can the NRC support in designing a roadmap for ensuring pay disparities are lowered in the coming years?
- ? What are considerations for the NRC to understand the market drivers for talent attraction?

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Changing trends in executive renumeration

Executive renumeration has been an important topic of discussion in India for many years. The trends in executive compensation have changed over time, reflecting changes in the economy, regulatory environment, and corporate governance practices.

There is an increasing use of performance-based pay in India with a significant portion of executive compensation tied to the company's financial performance, such as revenue growth or profitability. This trend reflects a growing emphasis on meritocracy and performance-based incentives.

Furthermore, there is a continuous decline in cash salaries and increasing prevalence of equity-based incentive plans for executives. This aims to align the interests of executives with those of shareholders and encourages long-term thinking and commitment to the company's success. As ESG and sustainability continue to gain momentum, there is a growing trend in India towards incorporating ESG factors into executive compensation. This reflects a broader shift towards sustainable business practices and a recognition that companies must operate in a way that benefits all stakeholders, not just shareholders.

Transparency and disclosure continue to be of great significance particularly in relation to board and executive compensation. Investors, regulators, and other stakeholders are calling for greater clarity around how executive compensation is determined and what metrics are used to evaluate performance.

These changing trends in executive compensation in India reflect a growing emphasis on performance, sustainability, and transparency. As the Indian economy continues to grow and evolve, it is likely that executive compensation practices will continue to evolve as well, with a greater focus on accountability, stakeholder value, and responsible governance.

Questions to consider:

- What are the key aspects which are prioritised with respect to executive compensated?
- How is executive compensation linked to board performance and its efficacy?
- How can the NRC leverage board evaluation outcomes to calibrate executive compensation?

Evolving frameworks for performance management of the board

Performance management of corporate boards is an evolving area, and boards must adapt to changing business environment and stakeholder expectations to remain effective and relevant. There are multiple frameworks that may be deployed for effective management of performance of the board, and it is essential that the board is well informed and competent to take critical and sensitive business decisions which may have long term ramifications.

Tools such as board self-assessment through interviews and surveys help boards to identify areas of strength and weakness and develop strategies for improvement. Additionally, external evaluations are also a methodology to review the performance of the board. Alongside the same, setting robust Key Performance Indicators (KPI) linked to business (short and long term) will be essential for progress tracking and identification of areas of improvement.

What are the key parameters that need to be tracked for the board and executives? How is it currently done?

Questions to consider:

- What are the key variables to be considered for an effective performance management framework?
- What are the capability parameters to be considered for ensuring effective decision making from the board?

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Succession planning

Succession planning at the executive level continues to be an evergreen agenda for the board, which has now become even more pertinent in BANI world (brittle, anxious, nonlinear and incomprehensible world). Organisations need the right talent at the top which can navigate businesses through the existing volatility. It is thus crucial to have the right internal and external pipeline of talent as a business continuity imperative for the organisation.

Successors may be identified from 'rising stars' who have dealt with the impacts of the crisis and those that sit on multiple boards and can share insights from their experience with other organisations. The trend for boards to identify talented individuals to become 'board apprentices' to observe the boardroom and provide independent feedback, as well as gain valuable training to reach board level is increasing.

Identification of critical leadership positions and drafting a clear objective evaluation criteria for potential candidates is crucial to enable effective succession and business continuity.

Board and executive evaluation constitutes a key part of this process. Regular and effective evaluation of executives and creating development journeys for candidates in the succession pipeline continues to be in the NRC's agenda this year. On a related note, NRCs should, as far as possible, seek to preserve stability at the top of the organisation by avoiding appointing the Chair and CEO in quick succession, where the two roles are served by different individuals. Similarly, NRC should, as far as possible, manage the retirement of board members to avoid losing too much 'corporate memory' in one go.

Questions to consider:

- What parameters are considered by the NRC while evaluating candidates for executive succession?
- What are the norms set and followed by the board on executive succession planning?

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