

# Board Assessment



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A Board Evaluation is a formal review process to assess the effectiveness of the board, its members and its committees.

## IMPORTANCE OF BOARD EVALUATION

The evaluation is required to ensure that the board is functioning efficiently in fulfilling its role and responsibilities. Board's decisions must align with the organization's long term goals. These evaluations are now an essential part of good governance, regulatory compliance and investor confidence.

Board evaluation has become a priority only in recent years. In words of Professor Jeffrey Sonnenfeld, who said in 2002: "I can't think of a single work group whose performance gets assessed less rigorously than Corporate Boards." However since then the situation has changed significantly.

Board evaluation is also being increasingly considered by investors in rating the governing standards of companies. An effective board evaluation process demonstrates to the investors that the company is well governed and raises the profile and reputation of the company.

It provides a mechanism for the board and its members to receive feedback, do self-examination and take concrete steps to improve. A well conducted evaluation exercise can recognise and correct corporate governance problems and contribute significantly to improvement of performance of the board and directors.

There is also pressure from regulators and proxy advisors for regular review of board performance.

## CHALLENGES IN BOARD EVALUATION

It is not uncommon to see caution and resistance to Board Evaluation. Defensive attitudes emanating from mind sets, egos, status, relationships and competence may make the process unproductive. Directors who have been on the same board for a long period may be uncomfortable judging or being judged. Some directors may fear that evaluation results will bring out their lack of expertise in IT, Financial or other technical areas and may be used against them.

In quite a few organizations we see form filling exercise that meets the regulatory requirements but does little to really meet objectives of a good evaluation. In such cases one typically finds all directors have same or similar scores which are at or near the highest rating score.

In IAAS-NSE Publication "Board Evaluation in India – Disclosure and Practices", Sonny Iqbal states "Only a handful of Indian companies undertake external board reviews and many others only engage in reviews to meet

the minimum requirements imposed by regulators. This results in routine reviews that evaluate basic objective metrics.... These evaluations are lengthy questionnaires, usually conducted by the Company Secretary or HR in partnership with the Nomination and Remuneration Committee. These exercises screen for problems rather than optimize performance and often result in high scores with few actionable suggestions for improvement. Additionally, hardly any Indian Company discloses areas for improvement that have been flagged during the evaluation and improved upon subsequently.

## INTERNATIONAL RECOMMENDATIONS

**G20/OECD Principles of Corporate Governance 2023– V.E.4** – Boards should regularly carry out evaluations to appraise their performance and assess whether they possess the right mix of background and competences, including with respect to gender and other forms of diversity.

## ICGN Global Governance Principles 2020 – 1.1 (I)

– In fulfilling their role effectively board members are responsible for conducting an objective evaluation of the board chair, board as a whole, committees and individual directors on an annual basis, including an external review at least once every three years.

## UK Corporate Governance Code 2024 – Provisions 21-22

– There should be a formal and rigorous annual review of the performance of the board, its committees, the chair and individual directors. The chair should commission a regular externally facilitated board performance review. In FTSE 350 companies this should happen at least every three years. The external reviewer should be identified in the annual report and a statement made about any connection it has with the company or individual directors. The chair should act on the results of the board performance review by recognising the strengths and addressing any weaknesses of the board. Each director should engage with the process and take appropriate action when development needs have been identified.

## REGULATORY REQUIREMENTS IN INDIA

Evaluation of Board, its Committees and Directors is mandatory for all listed companies. Some important regulations are listed below.

- Section 134 (3) (p) of Companies Act** – Report by its Board of Directors shall include a statement indicating the manner in which formal annual evaluation of the performance of the Board, its Committees and of individual directors has been made.
- Section 178 (2) of Companies Act** – The Nomination and Remuneration committee shall specify the manner for effective evaluation of performance of Board, its committee and individual directors to be carried out either by the Board, by the Nomination and Remuneration Committee or by an independent external agency and review its implantation and compliance.

- 3) **Reg. 17(10) of LODR** – The evaluation of independent directors shall be done by the entire board of directors which shall include –
  - a) performance of the directors; and
  - b) fulfilment of the independence criteria as specified in these regulations and their independence from the management.
- 4) **Schedule IV (VII) (3) of Companies Act** – The meeting (of only independent directors) shall
  - a) review the performance of non-independent directors and the Board as a whole;
  - b) review the performance of the Chairperson of the company, taking into account the views of the executive directors and non-executive directors;
- 5) **Schedule IV (VIII) (1) of Companies Act** – The performance evaluation of the independent directors shall be done by the entire Board of Directors, excluding the director being evaluated.
- 6) **Regulation 4 (2) (f) (ii) (9) of LODR** – Key functions of the Board of Directors – Monitoring & Reviewing board of director's evaluation framework.
- 7) **Schedule II (D) (2) of LODR** – The role of Nomination and Remuneration committee shall, inter-alia, include formulation of criteria for evaluation of performance of independent directors and the board of directors.
- 8) **Schedule V (C) (4) (d) of LODR** – The Corporate Governance Report shall disclose performance evaluation criteria for independent directors.

## ESSENTIAL COMPONENTS

### 1. Performance

- Achievement of organization's objectives.
- Strategic leadership.
- Financial Oversight.
- Risk Management.
- Succession Planning.
- Acting in the interest of all stakeholders.
- Crisis Management.

### 2. Policies and Procedures

- Frequency of Board Meetings.
- Quality and adequateness of Agenda papers. Circulation of agenda much in advance.
- Structures, policies and procedures implemented by Board.
- Use of external experts, consultants and auditors to aid the Board in decision making.
- Logistical Arrangements – Venue, Format, Starting Time, Duration – to facilitate productive discussions and deliberations.
- Tracking of items outstanding from previous meetings.
- Clear, comprehensive and accurate recording of minutes. Appropriate recording of dissenting views if any.

### 3. Board Composition

- Skill, Knowledge and Experience collectively.
- Diversity in Gender, Age, Professional Background & Cultural Background.
- Structure, terms of reference and effectiveness of committees of the Board.
- Independent directors to be truly independent.

## 4. Compliance

- Total adherence to legal and regulatory requirements.
- Use of tools to monitor compliances as the complexity and number of compliances required is onerous.
- Keeping up to date with changing laws.
- Chief compliance officer to give a report directly to the Board.

## 5. Governance

- Commitment to best practices in Corporate Governance.
- Ethical Conduct. Acting with Integrity. Objectivity.
- Interpersonal dynamics between members as also between Board and Management.
- Open and respectful discussion encouraging directors to contribute actively.
- Constructive handling of dissent and resolution of conflicts.
- Collaborative Decision Making.
- Managing conflicts of interest.

## 6. Training & Development

- Induction training for new members.
- Ongoing education and professional development of members.
- Interaction with senior team one level below the CEO.
- Visits to workshops, factories and offices to get first hand feel of the company's operations.
- Attendance record. Preparation and participation in discussions and decision making.

## INTERNAL OR EXTERNAL EVALUATORS

The evaluation can be done internally by a committee of the Board or by each member for other members. However it should not become a routine ticking the box exercise where everyone gives everyone else a good score either to expect reciprocity or avoid negativity. It is recommended that an independent consultant, who specializes in Corporate Governance and Board Evaluation and who can bring in objectivity and industry benchmarks & standards, while ensuring anonymity where required, is used periodically.

## FREQUENCY

Regular board evaluation is critical in keeping the Board agile & responsive and well equipped to guide the organization towards success. A comprehensive evaluation must be done at least once a year. It can be supplemented by specific assessments during the year for instance to measure the improvement in filling gaps identified in the earlier evaluations.

## OTHER BEST PRACTICES IN BOARD EVALUATION

- Design a structured framework for evaluation to ensure that all areas are covered comprehensively
- To ensure honest and constructive feedback, an environment of openness has to be created.
- If members are reluctant to give critical feedback fearing that it would go back to the concerned person and would create issues, the organization should consider hiring external experts and ensure anonymity.
- The process must give clear and implementable

recommendations especially in board training and development initiatives. It should identify gaps in

skills and perspectives that must be filled.

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#### REFERENCES

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