

# Boards' New Manifesto - Improving oversight on Human Capital Issues



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It is trite to say that Human Capital Management (HCM) is the most important function of any organisation. Although this concern is touted as the most important one in the annual reports the sad reality is that in a majority of organisations, HCM concerns remain on the periphery of corporate strategy.

Many things have changed in the last two years after the pandemic. For example, HR functionaries faced new

and unprecedented challenges such as mental health issues of employees, work from home and attendant problems, issues relating to engagement and retention and of course the great resignations. HR which normally rested within 'Management domain' escalated to corporate Board rooms for obvious reasons as it required fundamental shift in the working and realignment of traditional work and working methodologies. Employees mental health and tragedies in their families had different kind of implications. Issues of compassion and increasing attention to employee matters became subject of Board room discussions and increase level of corporate actions. It is hoped that these initiatives and attention and engagement of the top will become core part of HR strategy. As we adjust to near normal situation post pandemic, one thing is for sure that corporations have to be increasingly focused on human capital management (HCM) issues.

It is now evident that Disruption is a new normal and has the potential to create recurring turbulence in organisations. Research suggests that organisations can derive competitive and strategic advantage through superior management of intangible assets. Various intangible assets such as customer service, innovations and digitalisation are more, if not exclusively, amenable to human resources, as opposed to financial or physical capital. As an example, in the case of the financial sector, traditional risks such as poor credit decisions, slow adoption of technology, failure to manage NPAs, unsatisfactory customer orientation and leadership deficit need to be reframed as shadows or derivatives of the 'real' risk, namely inadequate human capital and a rigid bureaucratic culture. This makes it both necessary and urgent at senior (Board) and strategic levels to focus on accountability with respect to the use and effectiveness of human capital.

Traditionally, in the overall scheme of governance, regulatory compliance, adherence to best accounting standards and superior levels of ethical practices have found a prominent place in the Board rooms. Human capital, which plays a critical role in maintaining sound

governance has, at best, received a casual and peripheral attention of the Board. Most Boards with some exception have usually played a benign role in rubber stamping management proposals on HR and have generally shied away from overseeing the HR function perhaps to protect the autonomy of the management and with a view to avoiding overstepping into the latter's role. But the risk is significant whereby the business driven CEOs, eager to produce short-term results, may in fact ignore focusing on human capital issues which demand considerable efforts and time and persist with status quoist policies or, at best, introduce ad-hoc measures to meet the exigencies. A case in point is the failure to take effective measures by the management to streamline many tradition bound personnel policies stymieing professional and meritocratic system of human capital management. Failure of Boards to take notice and facilitate a new order can have severe adverse impact on the overall governance and business outcomes. There are other factors that may contribute to HR risks such as lack of professionalisation of the HR function, ambiguous and ad-hoc approach to building talent, etc.

Thus, there is a clear role for Boards to oversee and ensure (of course not through interference in the day to day HR management) that the Boards of the companies that they sit on have a robust Human Capital Management framework as opposed to merely rubber stamping issues placed before the Board in this vital area. They should lay clear policy perspectives and take strategic initiatives to ensure that human capital strategy is closely interwoven with business strategy. Besides, Boards should identify HR risks in their respective companies and monitor such risks from time to time like any other business risks. The role of the Boards is to use its collective wisdom to direct the patterned thinking concerning people issues to futuristic and global best practices, thereby putting in place a meritocratic system and humanistic culture.

Boards will need to address the under mentioned areas in HCM and endeavour to ensure the following:

- 1. Building HR assets:** Building HR assets involves building human resource competencies in HR functionaries more so if the function is not professionalised and is handled by operating managers as is largely the case in the financial sector, including in most PSBs. Boards need to ensure that their companies have strategic framework for human resource issues and supporting structures and resources. The Chair of the Board and CEOs have a special responsibility to lend support to HR function in using innovative methodology and global best practices in performance management, engagement and building leadership at various levels. A great number of leading Indian business conglomerates like Tatas, Aditya Birla Group, Wipro, HUL, Infosys, Mahindras and such like have made significant transformation of their businesses by building a high degree of professionalisation in HR and supporting their initiatives.

**2. Building Culture:** It is the main role of a CEO and the top teams to build a culture that manifests itself in courteous dealing with customers, ensuring quality standards in products and services, responsiveness, effective problem-solving processes and maintaining fair dealings in business at all times. For example, a culture of control and compliance can breed a culture of fear, indecisiveness and procrastination. Thus, culture shaping for Boards is very critical alongside their focus on regulatory compliance. As Boards have a critical role in reviewing the performance of CEO and the top teams, it will be a legitimate expectation that performance assessment is not based merely on business parameters but should include their contribution in building a positive culture and putting in place the best practices in HCM.

This is neither an esoteric endeavour nor overstepping their role but a fair expectation to meet the competitive challenges. The challenge before Boards is also to consider some of the cultural trade-offs as identified by the Association of Chartered Certified Accountants (ACCA) in 2014 and develop clarity about their own approach on some of the following issues:

- Values as a wealth-driver versus values as a protector
- Openness to mistakes vs tolerance
- Common-sense vs rules and procedures
- Innovation vs control
- Risk taking vs risk avoidance
- Trust vs accountability
- Human capital vs human costs
- Quantitative measures vs qualitative measures

**3. Building Oversight Mechanism:** It may perhaps be a little too much to expect Boards to devote all the energy and time required to guide management in building HR assets and create an architecture of positive culture. Yet, it is important for the Boards to provide guidance and oversight in creating a robust edifice of human capital management systems.

One of the functional ways to achieve this is to create a sub-committee of the Board, to advise and assist it on strategic HR issues by concerning itself with key roles including

- Help develop a strategic vision for HR, while providing the basis for integrating the HR strategy with the business strategy
- Undertake annual HR audit, climate and culture surveys, etc., to diagnose the areas of concerns and take appropriate steps
- Assist in building learning infrastructure to ensure all round development of human resources
- Review issues relating to talent, capability building and leadership
- Initiate measures to improve employee engagement
- Suggest measures to use increasing level of digitalisation for efficiency and effectiveness of various HR sub-systems.

This sub-committee can make significant contribution in moving HR issues from the periphery to centre in Board processes and take effective steps to insulate companies against any possible HR risks.

The author's experience in setting up HR committee of the Board in his role as ED and CMD of a large Public Sector Bank, much before constitution of such a committee was mandated by the Government, as a recommendation of committee on HR for PSBs chaired by the author, (popularly known as Khandelwal Committee) helped immensely in developing a strategic approach to manage HR function. The engagement of the Board members was very positive and HR played a very proactive role in the transformation process of the institution and extra-ordinary business growth. In fact, the HR sub-committee has become a major instrumentality for piloting HR transformation, thereby enabling the Bank achieve its various business goals. The HR sub-committee set up by the author in the Bank has continued for nearly two decades and has, over the years, been instrumental for many significant initiatives in leadership building, employee engagement, performance management and welfare.

A word of caution. Mere setting up of a Board committee is never adequate unless the CEO or the Chair of the Board is committed to making such a system effective. This can best be achieved by periodically holding its meetings, inviting expert HR professionals as special invitees and benefitting from their expertise and experience, exclusively focusing on strategic issues and avoiding its use for seeking approvals on routine HR administrative matters, commencing HR audit to diagnose the issues for undertaking reforms in HR policies, etc. Today, many CPSE's have a Board's committee on HR, which is a significant initiative but the more important issue is how the CEOs and the Boards take advantage of such a committee in shaping HR policies and strategies. Prof TV Rao, a well known HR expert and former Professor, IIM-A observes:

*HR committees of Board can play a significant role if it is not used for routine approvals of HR issues and CEO in particular uses the expertise of its external members effectively.*

It is thus evident that HR committees of the Board can become a powerful mechanism to shape and prepare in building a sustainable organisation provided they are designed to play only strategic role and the CEO puts it as a priority item in his scheme of things.

**Enhancing HR competence in the Board:** In recent times, many Boards have expanded their own competence base by inducting professionals from technology and finance areas. While this a welcome change, it is also necessary to bring in HCM expertise on the Boards which can contribute effectively in the deliberations of the Board. Other Directors must also be conversant, if not fluent, in the topic. It is the collective passion of the Board in building the architecture of human capital that would shape the company's culture. Board's contribution in HCM issues can substantially help develop unique competitive advantage for the company. New competencies in the Boards to meet new challenges can create new opportunities for growth and development of the companies.

**Improving HR reporting and disclosures:** Under the Environmental, Social and Governance (ESG) framework, SEBI has introduced the Business Responsibility and

Sustainability Report(BSSR)and made it mandatory from 2022-23 for the top 1000 listed companies by market capitalisation. The BSSR is aimed at securing transparent and standardised disclosures by companies on their ESG parameters which include reporting on various parameters germane to HR like gender and social diversity, turnover rates, welfare, occupational and safety issues and trainings.

This is a positive step but this is the minimum . Boards of companies can take pro-active steps to disclose many dimensions of their HR initiatives like employee demographics, measures for building leadership and succession, diversity structure, level of professionalisation of HR function, employee engagement and grievance handling mechanisms, learning and capability development, industrial relations, functioning and major decisions by HR committee, etc. Many organisations report on these issues in their own way. There is no standardised format for reporting and thus, it is difficult to compare the performance on such issues. It may be useful to make HR reporting by large companies mandatory like the reporting on governance. This will help catapult Human Capital Management issues as a central concern of the Board like other business and governance issues. Increasing level of disclosures on human capital issues can help attracting new investments .A collateral advantage of this can be increasing attention of the Boards and corporate managements to human capital issues and strengthening their respective companies as a company is as strong as its stock of human talent. Indeed, effective HCM disclosure

itself can significantly enhance shareholder value.

**Conclusion:** Board’s role is strategic in overseeing the overall performance of the company by focusing on a wide range of new initiatives including issues of inclusivity, gender balance, ethical excellence, etc. while, at the same time, remaining on top in delivery of service and meeting the needs of various stakeholders. **The achievement of corporate goals will depend on the relentless efforts by the company Boards and the respective top managements in enhancing their time and resource commitment to build ‘Human Capital’ edifice of their companies to respond to the new wave of disruption. Creating leadership and building culture to thrive requires most extraordinary attention at the top.**

It may be a challenge for Boards as to how deeply to be involved in HCM, and there are risks in overstepping into the managerial role. But, companies can not afford to ignore the talent and leadership issues given the risks that can appear on account of deficit talent / leadership and also a mediocre culture for change. it is, therefore, time that Boards improve their engagement and oversight on HCM issues. Boards of companies will not only derive long-term value, but also provide a template for how Boards can tackle other ESG areas. **Boards need to move from guardians of compliance to gate keepers of building intangibles, especially HCM, to build sustainability and growth.**

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