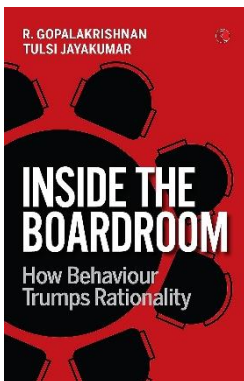


Blog + Book extract

INSIDE THE BOARDROOM: How behaviour trumps rationality

This book is about human behaviour. The title suggests that the examples are set in corporates and company boardrooms. That is only partly true. The narrative applies to sports bodies, NGOs, public bodies and any group of people tasked to lead an organization (- due to the background of both authors, the context of this book has been set in the company boardroom). In this blog, the R Gopalakrishnan and Tulsi Jayakumar, the authors, daringly suggest that directors are not entirely rational.



Knowledge of accounting rules and governance regulations account for only a part of good board directorship. All directors are human beings and are about as rational as other human beings. There is a fair element of subjectivity and behaviour bias while they make decisions. It is not difficult for directors to learn, or to be trained on, the rules and regulations regarding company governance. It is far more challenging for them to learn or be trained on rationality in boardroom behaviour. Behaviour is always self-taught, and it must be learned by each director. Nomination committees tend to recruit new board members for skills. They must perhaps give greater emphasis on recruiting directors for healthy attitude and constructive board behaviour.

It is human nature to seek power, prestige, and status. Hence our behaviours are those that can bring us respect, approval, admiration, and status. We intensely desire to fit in with people like us, and, once we are in such a group, we intensely desire to be prominent. This is why we tend to emulate behaviours of those whom we admire, or those whom we aspire to become. Newly appointed directors on boards display this tendency and motivation in spades. The new director, who sought to be a member of the board, has a strong desire to be an active member of the club.

We generate strong internal pressure to belong within the group. The benefit of being accepted is far greater than the benefit of being right, or cautious. These natural drivers and habits direct our functioning as board members. That is why behaviour often trumps the regulations and laws that define the role of the independent director, the board chairman, and the myriads of dos and don'ts.

Corporate governance is a recent coinage, dating to the early 1990s. Many people are unclear about what it really means, and some do not care.

Corporate governance is a code of rules and processes concerning how corporations should be managed for fairness to all stakeholders - customers, community, vendors, shareholders, and so on. India has been responsive to adapting and adopting international codes and practices. India has progressed but needs to do better.

Where is the elephant in the room - the big missing piece? The elephant in the room is invisible and undiscussed - human behaviour.

Just as we see the same face of the moon from earth, we see and debate the visible face of corporate governance - legal, accounting, rules, and processes. These are crucially important; they are necessary but not sufficient! The field of practice and public discourse is dominated by regulators, accountants, and lawyers. Where are the perspectives of the practitioners, the 'real' directors, who sit on boards for a fair part of their time? These perspectives are not missing, but they are thin in density. It is this gap that this book seeks to occupy by making the invisible visible.

The invisible face of corporate governance is board dynamics and directors' behaviour in the boardroom. How do directors interact, socialize, and arrive at viewpoints and decisions? Every board has its idiosyncratic social dynamics, and these influence mindsets and approaches.

Our book *INSIDE THE BOARDROOM: How behaviour trumps rationality*, explores this hidden side of corporate governance. Indeed, human behaviour influences decisions and responses not only in board rooms, but also in public administration, family managed enterprises, and even charitable organizations and gymkhana.

One point that the book sets forth forcefully is about prodromes. A prodrome is the symptom, the signs that precede the main event, like dark clouds or cool breeze before a heavy shower. Boards are comprised of powerful people - CEO, executive directors, and independent directors. If a company seems headed in the wrong direction due to the behavioural attributes of leaders, is it possible to read and interpret the prodromes? We believe it is possible to read and interpret the prodromes and that boards should act on their unproven but bothersome readings of the prodromes. We prescribe a 7-Ds series of steps in their book: descry-debate-demur-disagree-distance-depart-disclose.

Another feature of the book is the "Prodromal Test." It is a bit like the old Reader's Digest feature titled '*IT Pays To Increase Your Word Power.*' There are 15 questions to test prodromal signals. If you score over 10 for a company Y, you are advised to reconsider your association with the company. If between 6 to 9, you are advised to be observant and cautious. Is it a precise map which has rigour? No, not on this kind of subject. It is merely a compass, which can alert you if your direction is not pointing

the right way. It may be interesting for the reader to apply the test to a few companies to see if the test appears relevant.

Another idea outlined in the book is 'fly on the wall', extracted below.

Book extract

'The fly-on-the-wall' idea

To accomplish continuous improvement in boards, the tick box method provides some data. However, it tells only a part of the story. There is not available a neutral 'fly-on-the wall' person who can unravel the delicacies of interpersonal relationships, collaboration versus competitiveness instincts, and to get more for less.

Who can hold a mirror, true and faithful, to behavioural dynamics to the board as a whole?

The chairman of one reputed company approached Gopal to work with his board and senior leadership team to unravel the true potential of the talent in the board and senior team. Gopal worked with about thirty senior and experienced individuals as a Board Advisor for several months. The client company was happy not only to pay the fees, but to also soldier on with addressing the perceptual and psychological blockages that were diluting their potential impact. At the end of the engagement, those concerned were satisfied that the process was effective.

Initially we assumed that a great board is an assembly of top-class professionals. Indeed, regulations are also based on this belief: surely, distinguished professionals from bureaucracy and management must make effective board members. This is so only if their mind is 'prepared'.

Top class people need melding to be effective, they need to be a team, just as in sports. Dysfunction appears when you have 'personally accomplished, but team-underprepared professionals.'

Sports teams have coaches and mentors, so do modern top executives, but boards do not.

Boards can be noisy parliaments and might even appear dysfunctional due to conflicting views. Depending on personality, some do not speak up at all, some do so politely, while some others argue forcefully. Boards do not necessarily have a harmonious atmosphere, never mind the mythology that promotes such an image.

As we reflect on boards, the influence of human behaviour on board processes flash through our minds. Three anecdotes are relevant.

In one company with marquee directors, a management proposal to invest in an overseas fertilizer company was desultorily debated for many months despite unexpressed reservations among individual directors about the stability of the investee country. Directors interpreted that the chairman was keen on the investment. When finally, the chairman expressed reservations about the country, everybody chimed in, thus ceasing further consideration of the proposal.

In another board, the chairman himself piloted a proposal to invest in an unrelated diversification, hence big-name directors hesitated to oppose the proposal. A feisty and argumentative director, known to be a chairman-confidante, opposed the proposal vehemently to the great relief of the other directors.

In a third company, an ambitious CEO created the perception among his board that his edgy proposals had prior assent of a powerful promoter non-director. One day, they discovered that the edgy schemes were a massive fraud. It was a pity that the edgy schemes went unchallenged for long.

Governance is perceived as an abstruse and technical subject, connecting the three dots of accounting, legal, and regulatory. Hence, thought leadership on governance has been dominated by accountants, lawyers, and company secretaries. A fourth dot, the element of human behaviour, is sorely missing in governance preparedness.

As every director has experienced, human foibles dominate board functioning---ego, rivalry, crucial silence, treating directorship as a prestigious privilege and so on.

Beneficial results can be accomplished if directors would either train themselves, or allow to be formally trained, to embrace behavioural principles and group dynamics. There is a place for board coaching by a wise and experienced person, acting as a fly on the wall. Such a person can help ease the inevitable dysfunctions in board dynamics. While boards engage with rational, left-brain matters, there exists a place for affection, esteem, and warmth!

Consider certain soft skills---(i) how to balance operational and strategic issues, (ii) how to disagree without becoming disagreeable, (iii) how to speak up when it really matters, (iv) how to genuinely listen to alternate views without being judgmental, (v) when to be transactional and when to be reflective and above all, (vi) how to avoid relapsing into delusional memories of “during my days as the big chief, I used to....”

The new era is dawning for good corporate governance. Corporate India needs wise and experienced directors, who are no more active on boards, and who can sit in board meetings as a fly-on-the wall. They can do for collective boards what executive coaches do for ascendant executives. Just a decade ago, having a personal coach was considered derogatory to the executive. Within a decade, trained coaches of varying competence have emerged. These days, executives wear their coaches as a badge of

pride. Such a skill has developed in boards in Europe and America and may become relevant in a few years as an aid to India Inc.

This book is intended to stimulate the thinking that Board Effectiveness, like Quality Control, is a line leader's job. Senior leaders must take a total systems approach rather than a unidimensional or bidimensional approach. The idea of a reliable 'fly-on-the-wall' consultant may well have arrived.



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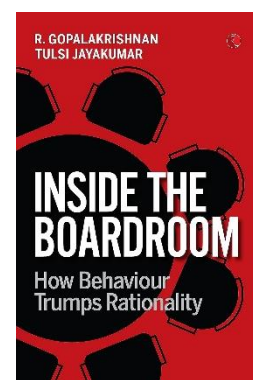


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This article contains the authors opinion and excerpts from his book. It is a commentary on the general trends and developments witnessed in the securities market.

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