

Importance of Succession Plans in Driving Sustainability–A Step towards Credible Governance



The recent spars in the Board Rooms of some leading organisations of Corporate India is a pointer to the absence of a robust succession plan in the senior most echelons of these Corporate. This vacuum in leadership talent impacts sustainable performance irrespective of size of entity or characteristics of business, whether family-owned, start-ups or established entities. The Companies Act 2013 has attempted to address this matter by defining the concept of Key Managerial Personnel (KMP) in safeguarding the brand image and meeting the expectations of stakeholders. Read on to know more...

Succession Planning Back in Spotlight

The *Times of India* in its article dated 25th October 2016, reflected on the subject of nurturing future



CA. R. Srivatsan

(The author is a member of the Institute. He can be reached at vatsan.rayam@gmail.com)

leaders, back up plans and challenges in building an environment of a cultural fit and a collaborative approach being important for every organisation. The article further reflected on “*The issues that stand out are the strength and independence of the board, the pressures brought to bear on chief executives in a complex and uncertain world, and the now established trend of the returning CEO. The cultural fit between the leader and his organisation and the lack of succession planning are also in the spotlight. CEO tenures have shortened across the world. While*

Members In Industry

pressure on performance at top levels is a given, the article underscores the dangers for large organizations which neglect succession planning and the mismatch between leaders and their teams. In addition to performance, collaboration and culture fit are equally important”.

Surrogate Leadership Vs. Trust Deficit

Is there a ‘trust deficit’ or ‘scarcity’ of trustworthy leaders’ amongst the young breed of professionals or is it a matter of transition where the first-generation entrepreneurs totally rely on the Key Managerial Personnel (KMP) to administer the organisation. There are many questions and factors that plague this void in identifying the ‘right successor’ or ‘maintaining continued trust’ and ‘avoiding conflicts’. Or is it the age of ‘surrogate’ leaderships that has dawned ‘Corporate India’ where the key investor or promoter has the reins and governance is stage managed and ‘Companies’ being eternally managed through remote controls. Any decision that is taken in the normal routine has the risk of being brought under scanner to be questioned at a later stage. Is it a situation of Key Managerial Personnel (KMP) being made a scapegoat eventually or is it a frightening scenario of an imminent ‘paralysis’ in governance?

Corporate Leadership Transitions

There are innumerable examples wherein companies with inadequate or inappropriate succession plans are exposed to vulnerabilities of closure, despite having the best of systems, processes, governance mechanisms and sustained value creation over decades of existence. Perhaps the biggest challenge is in ensuring smooth transitions in nurturing and

There are innumerable examples wherein companies with inadequate or inappropriate succession plans got exposed to vulnerabilities of closure, despite having the best of systems, processes, governance mechanisms and sustained value creation over decades of existence.

appointment of Key Managerial Personnel (KMP), Chief Operations Officers, Chief Executive Officers, in executive positions. In view of the recent regulatory development and ensuring effective governance, this succession plan may need to be extended to posts of directors and chairpersons of the board/operational committees.

The recent developments in large corporate houses

re-emphasise the need to include policies and framework on appointment of directors and a robust rotation policy, not being left to whims and fancies of few trusted individuals on behalf of the majority shareholders. Even where the Senior Managerial personnel are appointed as Directors or Corporate nominees, there must be a voluntary cooling period and avoidance of dual official positions within the organisation to remotely avoid conflicting business decisions. For example, a Company Secretary or a Chief Audit Executive or a KMP should preferably not be a director in any group company or vice versa. The trend seems to suggest that such conflict in roles as employee and as director could emerge as a major concern or dilemma leading potential litigations in questioning the independence in business decisions that impact the functioning of corporate entities in India.

Experience & Expertise minus Business Ethics = Risk Exposures

Historically, any corporate entity with decades of operation and family dominated business faces the challenges of ageing ‘functionaries’ predominantly nearing the age of superannuation. The trust and confidence of being an old timer being at a helm of affairs in such entities provide an eternal comfort to the stakeholders as well as a situation of indispensability of such functionaries. Boards of such companies are coerced to offer extensions in service and therefore engage them in contractual employment for an extended period due to paucity of trusted professionals/experienced administrators matching these trusted old-timers. Having reached a senior position and longstanding proximity to the board members, these are ‘giveaway perquisites in kind’ by corporate Houses for the lifetime contributions. This is the joint responsibility of the owners/promoters and the KMP to identify and nurture young talent.

Standardisation of Severance Pay for Top Executives

Whilst the Corporates are moving towards standardisation of severance pay for top executives, traditional companies are focussing on alternative methods. This includes extending the service period of superannuated executives. The next generation of top executives are likely to be more mobile in pursuing ambitions and would be ever ready to switch jobs as opportunities arise. To quote from the TNN report dated 27th October 2017, “leading IT Company has standardised its severance pay for

Members In Industry

top executives. For senior vice-presidents (SVPs) and executive vice-presidents (EVPs), it will be four months of their fixed salary. Severance pay had become a major bone of contention within the company over the past two years when seemingly arbitrary amounts were paid to former CFO and former general counsel. The CFO was granted ₹17 crore, while the latter, who was in the company for just two years, received \$868,250 (about ₹ 5.9 crore when he quit in January). The standardisation plugs the scope of individual negotiations. The CFO's pay-out allegedly went way beyond what his contract specified. The General Counsel's employment contract is said to have specified a severance pay of seven to eight months of fixed salary". These are pointers to future developments in Corporate India and frequent changes seems to be the new normal.

There is a paradoxical view on whether there is in reality a deficit of experts and professionals in the age of 35 to 60 years, as justified by the Boards in India for granting extensions and special privileges to corporate employees beyond the superannuation age of 58 or 60? Does this aspiration amongst those nearing retirement age result in certain unethical practices:

- by not working on a succession plan and evolving a successor much in advance of the retirement age
- Avoidance of 360° performance evaluation process, a norm in professionally managed corporate entities.
- By not ensuring an Independent propriety audit in such appointment and extensions, due to their loyal disposition.

Thus, there is a dilemma in succession plans faced by Corporate Entities in India on whether:

- a) offering extensions to trusted officials beyond superannuation for an extended period is justifiable for a smooth transition and assistance to successors
- b) appointing external professionals is a viable option to ensure independence in nurturing organisations and sustained growth.
- c) nurturing talent and leaders in a situation of high attrition, in retaining young talent
- d) Continuous monitoring of performance of Top Executives

The way the game of cricket has evolved, perhaps the transitions point out to various business formats in differentiating between the requirement for a 5 days test match, 1 day match and 20:20 matches. The players need to consistently perform and for any failure, there is always a back-up captain or player in the waiting. Corporate could perhaps draw an analogy in tuning the business as has happened in the game of cricket in all its varied dimensions.

The Paradox in Succession Plans

In recent years, the trend across industry indicates that employees reaching superannuation despite their loyal dispositions carry the stigma of having worked around the system that is grossly unjustified. The dilemma is to address the expectation gap in the mind of stakeholders in defining the rationale in Board Room discussions and remuneration packages offered to deserving roles in the organisation. The Companies Act, 2013 perhaps drives home the point towards greater transparency in the system in the manner in which the 'remuneration committees' and 'risk committees' operate and report the proceedings. The same is complemented by regulators such as SEBI, in bringing the right perspective in Board discussions and ensuring an 'arm's length' approach in justifying the decisions to the shareholders.

There is a perception that majority (influencing) stakeholders influence the working of compensation packages and remuneration offered to 'Top Serving Executives'. That the 'exit packages' are being scrutinised under the lens and often challenged with reference to delivering performance. In contrast, there is another challenge in 'refilling' the leadership positions, especially those have reached superannuation and are confidante of the management. Finding a suitable successor who matches with the organisation ethos & pathos brings in another set of challenges. The contrasting views and paradoxes in decisions, also pose a challenge on what constitutes adequacy on disclosure norms to regulators and in annual reports or even in the Directors Responsibility Statement.

Background Check specialists (duly supported by independent practicing Chartered Accountants/ Company Secretaries/Investor Analysts & Due diligence professionals) play an important role in studying the antecedents in deciphering the appropriateness of these decisions:

Members In Industry

The Companies Act, 2013 drives home the point towards greater transparency in the system in the manner in which the 'remuneration committees' and 'risk committees' operate and report the proceedings.

The same is complemented by regulators such as SEBI, in bringing the right perspective in Board discussions and ensuring an 'arm's length' approach in justifying the decisions to the shareholders.

- (i) in appointment of 'Top Executive' positions,
- (ii) in identifying a successor or
- (iii) in conducting propriety audits for 'top executive' exits/extensions.

These aid in decision making for the Board in the rationale behind the appointment, remunerations and planning for extensions to deserving 'Top Executives'. The due diligence exercise offers a ready reckoner aiding the Board decisions and could be even extended for appointment of Directors/independent Directors. The antecedents of these executives enable a rationale decision making and building an environment of 'confidence building' as part of the maintaining good investor relations.

Unlike Government Services, where there is a provision to discontinue or attach the pension income for any impropriety that is discovered or for any contingency, there is no such provision in the private sector and these are 'ab initio' form part of 'performance pay component'. Experience suggests that a wise counsel would prevail in 'earmarking part of the emoluments as contingency fund' or 'a clause' in the contractual arrangements for recourse to such 'authority' in case of post facto developments, for any form of impropriety. As the regulations do authorise for reopening of matters over an 8 to 15 years period retrospectively, especially the RBI regulations and those that relate to money laundering regulations. The Insolvency & bankruptcy code would be another factor that would bring to the fore the increasing responsibility and accountability on the 'Key Managerial Personnel' in terms of delivering performance. A balancing act is necessary to strengthen the line of defence for the corporate functionaries during their service and at the same time safeguard the interest of the stakeholders. May be an adequate 'professional indemnity cover' is desirable for the 'Top Executives'?

Remedial Measure in Driving Succession plans:

No person is eternal or indispensable in any professionally managed organisation and the cryptic view is that there is no dearth of 'talented professionals' across the globe and in India. There are about 2.8 lakh Chartered Accountants (and equal number of engineers and other specialists in industry). Yet there is a dearth of suitable leaders in identifying a suitable successor as organisation have a set of value system.

Clear advance planning would help in identifying a successor and provide a graceful exit to leaders those have served the organisation diligently. A rotation of roles and handover of charge to a successor 1 or 2 years prior to retirement is normally followed in professional management organisation and provides an incubation period for the new leader to understand and adjust to the work eco-system.

Custodians of Stakeholder Trust

Another factor that is largely underplayed is that the banks and financial institutions are in a position of trust and are a custodian of funds for the stakeholders and when these are deployed with Corporate Houses as a conglomerate or syndication of loan, there is an element of trust deposited amongst these institutions. While a nominee director is represented in the Board as a result of these funding arrangements, any Corporate misadventure does get reflected through such representatives to the consortium banks. In these circumstances, the law is reasonable in providing comfort to Private operators and, therefore, there is an element of moderation in implementing the regulations:

- a) Differential treatment is given to public enterprise and those in private sector
- b) The whistle-blower policy as applicable to a public servant is not extended to officials operating in private sector (where the funding is done by government, banks and financial institutions those deal with public money).
- c) The RTI act is not be applied or extended to private sector and even to private company that use bank funds.

Watchful Glare of Regulators

Conflicting regulations and regulators pose a significant 'regulatory risk' in corporate sustainability. The 'activists' posing as those espousing the cause of 'professional social responsibility' are like hawks

Chartered

ePass
2003 Series Tokens

Celebrating **1** Cr ePass

THANK YOU

5 Years. 1,00,00,000 Tokens.

ePass wishes to celebrate the exemplary milestone in our continued journey of availability, quality, ease of use and excellence at affordable price!!

Words are certainly not enough to express our deep gratitude to our partners, well-wishers, RAs, & CAs for all their support, trust, love & guidance. This wouldn't have been possible without you! THANKS AGAIN!!



signer**digital**

Console | Server | API | Service | Browser Plug-in | Cloud HSM

www.signer.digital



For more details & DEMO call:

Delhi
011-45037177

Mumbai
022-28955888

Bangalore
080-40921639

Ahmedabad
079-40083529

Kolkata
033-40078356

Nagpur
0712-6638888

Members In Industry

Another factor that is largely underplayed is **that the banks and financial institutions are in a** position of trust and are a custodian of funds for the stakeholders and when these are deployed with Corporate Houses as a conglomerate or syndication of loan, there is an element of trust deposited amongst these institutions.

waiting to take a plunge into the mayhem of 'mis-governance' with the slightest of tremors that shake the top echelons of the corporate functionaries. The stringent regulatory norms and evolving role of regulators, though dormant in the normal functioning of corporates, rise like a dragon when faced with a conflict amongst the differential vested interest of stakeholders in their role as promoters, major and minority shareholders, debtors, lenders, creditors and even disgruntled employees who at times turn out to be the whistle-blowers.

The provisions of section 199 of the Companies Act 2013 may be put to use for proper risk allocations.

Section 199- Recovery of Managerial Remuneration in Certain Cases

This is a new provision introduced in the Companies Act 2013. It provides for recovery of remuneration including stock options received by the specified managerial personnel, where the benefits given to them are found to be in excess of what is reflected in the restated financial statements.

Compensation for Loss of Office of Managing OR Whole-time Director or Manager (Section 202)

There is a balancing act in enacting the legislations in protecting the interest of the corporate functionaries including Directors for loss of office or premature retirement under certain conditions.

The regulator seemingly would work towards greater empowerment of corporate entities, in being intrusive and questions matters relating to breach of trust, wrongdoing, criminal misfeasance that may not come under the direct purview of regulations, in safeguarding stakeholders' interest. For the purpose there is an element of liberal voluntary discretion given to Corporate Functionaries in reporting these incidents of wrongdoing under the Companies Act, 2013 and on other governance related matters.

In conducting inquiries and investigations, the regulator also grapples with bridging the conflict between the criminal law procedures that focuses on the offence and not where there is any personal

gain or loss to the perpetrator or on the Company? Hence a broader view would need to be drawn in prosecution matters in differentiation between criminal negligence, breach of trust and pecuniary gains (as governed by Civil law). These arguments may be endless and there is no eternal solution to gauge the real 'power centre' in matters relating to effective governance.

Notwithstanding the above contrasting views, a mature corporate entity would need to wake up to the ground reality of ensuring robust succession policy framework in countering the criticism of greed, opportunism and define the rationale in granting extensions to superannuated officials and those on dual official positions, thereby instilling an element of confidence in the stakeholders/Regulators.

A loyal caretaker (officials remaining in top executive positions for a considerable period of time) are to continue to play the role of 'Bheeshma pitamah' till such time, the reins are handed over to an able leader or administrator.

To conclude, there is a saying 'a stitch in time saves nine'. The timing rather than timeline has gained importance as the new norm. Corporate governance and business transformations have taken a new curve with the recent happenings in corporate world where 'the trust' has to be reinforced as between the stakeholders, the risk practitioners, the KMPs, Board and upholding the sanctity of independent Directors. The same is feasible only through an open honest communication amongst these constituents backed by transparent administration of Corporate Affairs and sound internal counselling measures. The 'fear of policing' would need to be dispensed with and a measured approach in avoiding conflicting roles

There is a saying 'a stitch in time saves nine'. The timing rather than timeline has gained importance as the new norm. Corporate governance and business transformations have taken a new curve with the recent happenings in corporate world where 'the trust' has to be reinforced as between the stakeholders, the risk practitioners, the KMPs, Board and upholding the sanctity of independent Directors.

would be a necessity. Decisions taken as part of fiduciary responsibility would need to be defensible under all circumstances and this would need to be duly balanced with requisite authority, responsibility and accountability. Where to draw the 'Lakshman-Rekha' is a matter of organisation ethos and pathos, inscribed in its value system. ■