

Advancing Board Diversity and Renewal

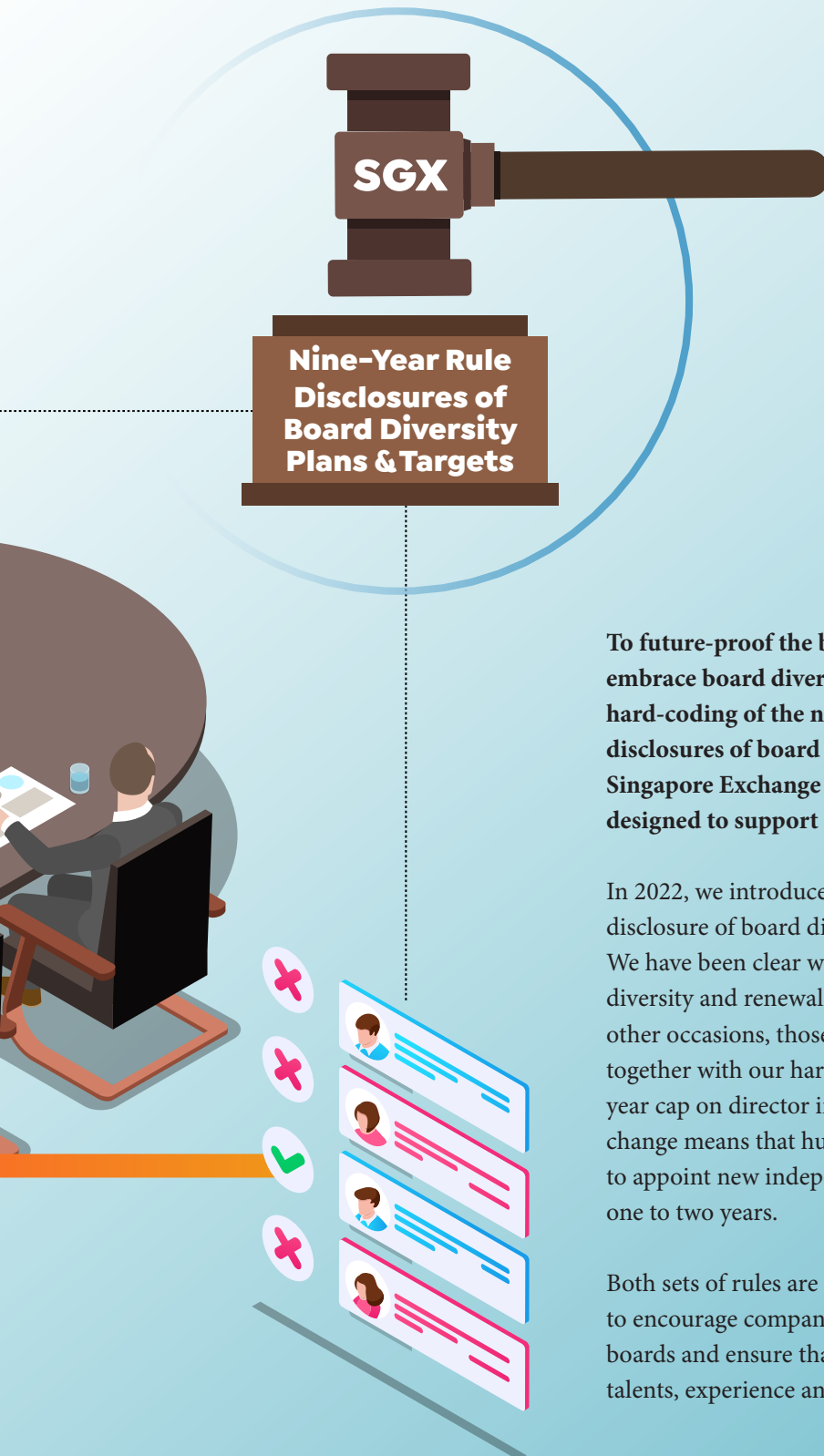


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REGULATOR'S VOICE





To future-proof the board, companies must embrace board diversity and board renewal. The hard-coding of the nine-year rule and mandatory disclosures of board diversity plans and targets by Singapore Exchange Regulation (SGX Regco) are designed to support organisational resilience.

In 2022, we introduced rules mandating the disclosure of board diversity plans and targets. We have been clear we want this to result in greater diversity and renewal. As we have explained on other occasions, those rule changes should be read together with our hard-coding in 2023 of the nine-year cap on director independence. The latter rule change means that hundreds of companies will have to appoint new independent directors in the coming one to two years.

Both sets of rules are designed to work in tandem to encourage companies to renew and refresh their boards and ensure that they have the necessary skills, talents, experience and diversity.

Diversity is valued, not for its own sake. We want diversity to enhance good decision-making by boards through the inclusion of additional perspectives that might not otherwise have been considered.

Cognitive diversity

In this regard, the parable of the blind men and the elephant is instructive. In this story, a group of blind men heard that an elephant was visiting their neighbourhood. None of them had encountered one before. Out of curiosity, they sought it out and touched it to try to understand what an elephant was.

The first, whose hand landed on the trunk, said, “This being is like a thick snake.” Another touched its ear and concluded it was like a kind of fan. The one who felt the leg thought the elephant was like a tree trunk. The man who placed his hand upon its side said the elephant was a wall. Another who felt its tail described it as a rope. The last felt its tusk and proclaimed the elephant was like a spear.

The point of this story is that each of these persons had an accurate albeit incomplete understanding of what an elephant is. But they are still better off than if they had spent all their time touching the same part of the elephant.

Shareholder preference

Besides the regulatory changes described above, another catalyst for greater diversity is shareholder preferences. Empirical research has found that “diverse” directors tend to attract higher levels of shareholder support.

SGX Group’s own experience bears this out. Our three most recently appointed board directors come from fairly uncommon backgrounds: one is a lawyer with extensive working experience with startups, another is a venture capital investor who used to work in private equity, and the third is a former politician. And at our most recent AGM, they received the highest positive votes of any director put up for re-election.

I do not want to overstate the point since all our directors received overwhelming shareholder support, and the differences are in the order of one to two percentage points. But, their relative outperformance does support the general finding of greater shareholder support for more “diverse” candidates.

An evolving landscape

The third catalyst for change is structural necessity forced upon us by our operating environment. The term “VUCA” or “volatile, uncertain, complex and ambiguous” describes the world that we live and work in. More recently, we have a new term: “BANI” or “brittle, anxious, non-linear and incomprehensible” to emphasise how much the world has changed.

To navigate this new environment, we need more of the different, not more of the same.

With this in mind, consider a board recruited only from the Old Boys’ Network. I think most, if not all, shareholders and indeed stakeholders will find that this just would not do – especially since we all come with our own limitations and biases that affect our understanding of the world and our decision-making.

The literature suggests that these biases persist even when we are aware of them. And the best way to combat their effects is to surround ourselves with trusted but alternative perspectives that can help us check our thinking.

Challenges

Having said that, I do acknowledge that the process of achieving greater diversity is not straightforward. There are some challenges.

First, there is the challenge of identifying what kind of diversity is desired. Companies should not be adopting a cookie-cutter approach but should be looking for candidates who meet their unique needs. In identifying those needs, some boards do a skills assessment or use matrices that give a full view of board skills and experiences and use this to evaluate where gaps need to be closed.

Others suggest that diversity should consider not just professional and technical expertise, or role and position of the candidate, but also their philosophy of life and interests. This holistic assessment then needs to be mapped to the company's goals. In other words, what is most important is to demonstrate how the diversity targets result in the skills, experience and values necessary to support the company's long-term strategic objectives.

To future-proof the company's business against disruption and meet the pressing challenges of the day, boards must be ready to tackle issues such as digital transformation, human capital and environmental, social and governance concerns.

The next challenge is finding and securing appropriate candidates that can meet those needs. Nominating Committees and incumbent directors would need to consciously take concrete steps to counteract the natural tendency to search within their usual networks and choose what feels familiar. A diversity of candidates can only come from a diversity of sources.

Some suggestions boards might want to consider would include engaging an external search firm or insisting that a diverse slate of candidates be presented for consideration. Directors can also consider sponsoring or mentoring diverse leaders, whether within their companies or through their extended networks. SID can assist in this process, through their search tools such as Board Match and Board Listing.

A third challenge is how to get a diverse board to get along and function effectively. The addition of new, diverse directors is likely to result in the introduction of different views, and can upend established group dynamics. The board will have to consciously encourage healthy board dynamics while integrating those new entrants to enable respectful debate on issues in a collegiate manner, while still making decisions in a timely fashion.

The 4CT tool developed by the Centre for Creative Leadership, which builds board collaboration, candour, challenge, commitment, and trust, is one example of the myriad tools that exist out there. The SID Listed Entity Director Programme for first-time directors supported by SGX has an entire module devoted to board dynamics. And for those who are interested in upskilling and preparing themselves for future roles, SID has launched Accreditation and Board Readiness Programmes.

Real change

We have implemented regulatory reforms to try to achieve real change, real renewal, and real succession planning. And we want to see such renewal and change across the entirety of our directorship landscape. We do know that our rules are not a recipe for, nor a guarantee of success.

Rules can catalyse the discussion in the boardroom and provide the necessary transparency for the market to scrutinise whether the board is doing enough to be diverse enough for the intents and purposes of the company. But achieving success requires companies to foster a corporate culture of diversity through sustained commitment.

A game of musical chairs would not help companies in their decision-making, would not benefit shareholders in delivering value, and would not uplift the quality of our market. We do not want to see this, so I hope for the cooperation of our entire market community.

This brings me to the final challenge: how do we measure progress?

Together with the Council for Board Diversity, SGX RegCo has recently launched a report on the state of board diversity disclosures. The report examines both the state of disclosures as a whole and the quality of their contents. The review also identifies laggards and explores ways to improve the overall and individual company performance. I believe the report is a helpful guide, and I commend it to your attention. ●