ICGN International Corporate Governance Network
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ICGN Seoul Conference – *Assessing Board Quality and effectiveness of CEO Oversight*
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- **Yuelin Yang, Chief Stewardship and Well Being Governance Officer, IMC Pan Asia Alliance & Deputy Group Managing Director, IMC Industrial Group & Group Managing Director, Unithai**
- **Christine Chow, Global Head of Stewardship, HSBC & Board Member HSBC GAM**
- **Jaeuk Khil, Professor of Finance, Hanyang University & Outside Director, Hyundai Glovis**
- **Luz Rodriguez, Director of Corporate Governance and Legal Services, Colorado PERA**

- **Chaired by Rajeev Peshawaria, Chief Executive Officer, Stewardship Asia Centre (SAC)**

Rajeev Peshawaria:
What are the most common pitfalls with board composition and how can they be remedied?

Yuelin Yang:
I'm a family member of a company. We've had great discussion about family business pros and cons. We view family businesses as HBO's Succession or Dynasty or Dallas, family politics and emotions. King Lear, dividing the pie equally, or between those most capable or loyal. Our family often joked about Prince Charles still waiting to succeed, or Rupert Murdoch's children. The Godfather, a non-family CEO or Independent Director facing Marlon Brando, Chairman, family head, Director and main shareholder, very difficult.

My life was half spent in US, then in Asia. Having worked extensively in US and been active in the Asian Corporate Governance Association, I'm well versed in Western corporate governance practices. I've spent the last 27 years in business for my uncle and now cousin. Family businesses are generational, about emotions and are more informal, corporates are business cycles, about economics and more institutionalised.

There are unique aspects to families as concentrated owners. There's no investment chain, but a group of owners. Sometimes the people are too engaged. Ideally, there's clear division between family and business governance. Separate the emotions and economics. Families shouldn't treat businesses like ATM machines. Corporate governance is horizontal, between family and minority shareholders, not vertical between management and dispersed owners. The family needs, but often doesn't have, good governance for share succession, future family leaders, dividends versus reinvestment, control versus growth and family employment policy.

Key Director attributes in family companies are extra soft skills when dealing with family owners. You must be trusted, but objective, a consigliere. Independent voices are more important in family companies for party transactions, family member compensation, etc.

Additionally, Directors are often buffers separating non-family management and owners, sometimes between family shareholders, and mediate disputes, particularly with active family members versus non-active shareholders. Sometimes you need to mentor and manage.

Christine Chow:
HSBC Asset Management is part of HSBC's Financial Services Group. We manage US $600 billion assets under management and cover passive and active businesses, and alternatives, e.g., infrastructure, venture capital and private equity.

I usually examine three things. The definition of board independence, distinguishing the hardware and software. Hardware is the numbers, independence number, CV and biography of Directors. Hardware makes machines look good, but software must also work. Board Directors need skill and character, to navigate political sensitivity in boardrooms and harness soft power. Engagement is necessary to assess soft skills, not just individually with Independent Directors. Best assessment is in ongoing interaction.

I recently met the first female board member in an Asian company. She attempted to answer questions at an investor roundtable. In her first year she was seeking reassurance from the Chair and Executives. Subsequently, she became more confident in her expertise and speaking up. Investors like Board Director dialogue, both individual and collective. Observing body language is important to evaluate relationships.

I also observe board skills. We increasingly see investors asking for published board evaluation summaries. The problem is financial literacy, but there are other skills and definitions aren't clearly defined. Historically, there were legal and accounting skills, very specific expectation of board skills. Increasingly, board skills involve ESG and sustainability. It's knowing which part is meant and how to distinguish ESG and sustainability. When I see Board Directors with cyber, IT, digital and AI skills, I think they're superheroes, because each is very different. All businesses have digital offerings, within which are different challenges. Understanding cybersecurity requires someone with government public security background. AI is a topic we've discussed extensively. It's about understanding the technology and mathematics.

When engaging with companies and Board Directors, we must assess their insight. Most board members get company information through board papers, which isn't enough. Most effective board members have alternative information sources, they visit the workplace, have connections with different levels of the organisation. You must have frontline interaction to ensure whether the company's culture is working.

Jaeuk Khil:
I teach finance and undertake research. I've been an external Director for SK Securities in Seoul from a decade, subsequently five years as Independent Director for Hyundai Glovis, both family firms. From personal experience, Independent Directors can do a lot, but individually, it's difficult to accomplish most things, you require board effectiveness. Individual board members need quality and skills, but

can accomplish more as a group, so group dynamics are different and more difficult. It's more complicated for family firms.

One remedy is the second and third largest shareholders recommending outside Directors to BoDs. This works better for monitoring and giving guidance to BoDs, determining board effectiveness. In Korea, the Woori Financial Group, controlled by government due to financial restructuring period difficulties, now have five or six Independent Directors from non-minority shareholders, 4% shareholders for financial firms. They have played constructive roles in monitoring management teams and providing strategic guidelines for the group activities. This influence might extend to other Asian countries controlled by family-run companies.

Luz Rodriguez:
I run corporate governance and proxy voting activities at PERA. Boards are focal points for corporate governance. Voting for Director nominees constitutes most ballot proposals. The expertise, skills and time commitments necessary for successful board members make this probably the most impactful decision. Colorado's policy advocates board independence, refreshment, diversity and shareholder responsiveness. The most common concern is selecting board members with the right purpose, vision, strategy, and having adequate diversity and thought to challenge management.

Corporate boards have issues removing ineffective board members. Annual self-assessments, covering performance and overall effectiveness, is key, alongside three-year independent third-party evaluations, as with ICGN. Skills, character and shareholder advocacy is essential.

Rajeev Peshawaria:
Board effectiveness is essentially skill and will. Three sustainable growth pillars to ensure sustainable growth are brains, bones and nerves. The brain is purpose, vision, mission, strategy, requiring deep familiarity with industry dynamics and technical expertise. Many boards perform poorly in this area. In McKinsey's survey of hundreds of international Directors, only 34% agreed their boards fully comprehended company strategy. 22% felt their boards were completely aware of how their firm creates value. 16% claimed they had strong understanding of their industry dynamics. We must pay attention to ensuring Board Directors create differentiated strategies.

Bones is people, processes and structure, having the right leaders, adequate performance, risk and reward processes, a structure appropriate for our fastmoving economy. Directors must understand organisational performance dynamics and ask appropriate questions.

Nerves is culture. Today everything organisations and individuals say is viewed publicly. The only competitive advantage is culture. Does the company have an ethical culture and are values continually lived? Executive compensation and values should be aligned. Boards need Directors who understand human capital dynamics and ask culture and value questions.

Next is will, whether Directors want to be there. Scandals like Theranos, Volkswagen and Boeing, they are not there. Theranos had Military Advisors, Politicians, Influencers, George Shultz and Henry Kissinger on board, with no medical device expertise. What is the motivation? Enron's board remained quiet on many questionable practices. In 2000, each was paid £350,000 in cash and stock, over twice the current average for Directors.

Brains, bones and nerves run companies. Are Directors deeply skilled in at least one and broadly in the others? Are they willing to sincerely discharge fiduciary responsibility?

Patrick Dunne:
Do boards have adequate data savvy, which differs from digital, cyber, interpretation, communication and interrogation of numbers?

Christine Chow:
It depends on data presentation. Whoever prepares board papers has an agenda for pushing items through board meetings. Many Directors are good at demanding more data, but aren't always smart in asking what data and how it should be presented, to gain insights. As we receive more data, Directors must specify what data they require, so they aren't misguided when considering companies' best interests.

Yuelin Yang:
As an Independent Director in consumer business, for Verlinfest (AB InBev shareholders). Is there an industry distinction? In shipping, it's opaque, but Verlinfest have data on consumer markets and studies. Consumer appears more transparent than heavy industry.

Jaeuk Khil:
Internal have more access to internal data detail than external Directors. Theoretically, there are many things to manage those situations, but in practice it's difficult. Managing data for structure and processes for BoDs must be carefully designed and regularly evaluated by Independent External Directors, which may be more helpful to data efficiency.

Luz Rodriguez:
Like shareholders, Directors must demand decision useful data. They receive extensive information, but it must be specific and decision useful.

Rajeev Peshawaria:
The best data advice I received was, "Don't be data driven, be data informed." Use judgment on top of data, because if everything's data driven, we'd be robots.

Cristina Ungureanu:
New Directors need cyber, AI skills, etc. Should overall board profiles, current Director characteristics, etc., complementary of skills, be considered?

Rajeev Peshawaria:
Individual Directors can't have all skills. We need complementarity. We should assess overall board skills.

Jana Jevcakova:
In many jurisdictions Chairs are CEO or Executives. Should Chair independence be regulated by law, regulator, stock exchange?

Rajeev Peshawaria:
BoD Chairs and CEOs are often the same person. What about independence and conflict of interest?

Rajeev Peshawaria:
In theory, governance model should be different Chairman and CEO. In practice, it often isn't. It may vary by situation, company life cycle, size, industry, cultural differences. Separate CEOs and Chairs are preferable to ensure independence on decisions. Differentiating CEO and Chair roles may be more efficient. With appropriate processes and structures, it may be less significant.

Yuelin Yang:
Family companies and possibly tech companies may be more extreme. I agree with my 96-year-old mother, Ambassador Tsao Yang, who firmly believes they should be separate.

Christine Chow:
Officially, Senior Independent Directors are best. From experience, on soft power boards it isn't necessarily Chairmen, but usually someone with influence, who harnesses board energy. Institutional investors are helpful for board composition clarity, but conversations with other Board Directors help us understand the underlying power dynamics and who has influence. Formal and informal engagement conversations reveal power dynamics and company direction.

Rajeev Peshawaria:
In North America there is a stronger joint CEO-Chairman model.
Luz Rodriguez:
US CEOs have bigger egos. They often negotiate to be both CEO and Chair. Institutional investors' policies advocate separation. It promotes management accountability and creates independent board leadership and unbiased board evaluations of CEO performance. Most policies support separation proposals, but the roles are commonly combined. When Jamie Dimon leaves JPMorgan, the role will no longer be combined.

Rajeev Peshawaria:
It's popular in Asia. We're beginning to see that more in the US. There are pros and cons. When CEOs are Chairs, there are speed advantages, etc. It reduces risks to have a process of board members evaluating Chair performance annually, without their involvement.

Huiwon Yang:
As an Analyst, I evaluate ESG in financial companies. What is the most important thing for board quality of financial companies?

Jaeuk Khil:
The first-time government controlled Woori Financial Group was because of financial restructuring process. They then went onto the open market, and five companies acquired full percentage share of Woori. They have rights to recommend Independent External Director to the BoD. The management is now five independent BoD members discussing and approve management decisions, acquiring financial subsidiaries and major business directions. It's a good example of financial companies maintaining good quality access, risk management and business practice. Financial companies require more by law and regulation to maintain board effectiveness and risk management security, but diverse BoDs from second/third shareholders, who have interest in company performance is good for management.

Rajeev Peshawaria:
Generally, what elements are most important for CEO selection and succession?

Yuelin Yang:
Monday's Financial Times states the Mars' non-family CEO, there for years, has connected well with three generations. The same issue with Suntory, three-generation family, with CEO Takeshi Niinami from Mitsubishi, and Bertelsman, Thomas Rabe crosses the field from his farm and talks to the owner. There are good success stories for non-family CEOs.

There are unique issues with family business succession, patriarch won't let go, nepotism versus meritocracy, next generation uninterested, unready or incapable, family politics. Families are undergoing maybe four or five transitions. Patriarchs leave, there's a new head and shares are transferred down. Non-family CEOs are another transition. Sometimes families must change mindset from owner Manager to own. There's also wealth management. My uncle passed and left substantial cash and real estate, alongside the family office. These transitions can happen concurrently.

It's difficult for family businesses to attract and retain non-family talent. When interviewing, I prefer people who've previously worked in family businesses. Families prioritise loyalty and seniority, so they need clarity on reasons for non-family management. Is the business in transition or crisis, growing in size and geography?

Drivers for non-family CEOs can be business growth, but sometimes in Europe, third/fourth generation companies, to avoid family politics management, is entirely external. Future generations are hopefully more open to outsiders and with globalisation, businesses demand new competencies.

Candidates should know whether families are ready for outsiders and if there's family governance. Candidates need soft skills to deal with real owners, where no investment chain is involved and align with individual family culture and chemistry. They must be long-term and understand family values, from reputation to family name.

Next generation family CEOs have advantages, from their family name, understanding family values, culture, to long-term thinking. Negatives are nepotism, their relative passion or obligation, readiness. There can be difficult attracting non-family management, with perceptions of non-family glass ceilings.

Rajeev Peshawaria:
Family business succession is a big element in Asia.

Christine Chow:
Infosys, India, had 14 founders, they welcomed an external CEO and benchmarked Executive remuneration to US levels. They had to bring an original founder back to sort the issues. Transition is never easy.

For CEO selection, we must be clear on task and adjust selection criteria. Except family generational promotions, CEOs have time limits. There could be a drive towards cultural change, resolving an issue, growing the business organically, mergers and acquisitions, or restructuring or resale. Without clarity you won't find the right person. Assess personal motivation, purpose and values, review previous history, track record, integrity. It's easy to impersonate someone else to acquire a role. Distinguish experience and skills and future expectations. Often in human capital or talent management we evaluate model employees using existing skillsets. Using statistical assessment is retrospective. Sometimes the skills required don't already exist in the company.

Jaeuk Khil:
In Korea there isn't an external CEO market. Most CEO candidates are raised within the family groups on farms, progressing through the levels, and are selected by characteristics. In theory, shareholders meetings choose BoD members, who choose CEOs. In practice, the CEO selects BoD members.

Luz Rodriguez:
Brains, bones and nerves also applies to CEOs. I agree with the points raised about brains, the skillset, nerves, culture, the right fit. Regarding the bones, a robust process is needed, which is discussed annually and mentioned when there are internal candidates, planning for emergency circumstances. Most apparent is the full board is responsible for CEO choice but picking Directors to lead the process is critical. A Canadian bank was recently selecting a new CEO. The Selection Committee had three leading internal candidates; all deemed a good fit. Two months after final pitches to the Selection Committee, the Co-Chair was named CEO, raising conflict of interest issues. Those assigned to lead the process are very important.

Rajeev Peshawaria:
Skills and willingness to take responsibility are basic stakes. Enforcing CEOs will not work. An issue more pertinent today than ever when selecting CEOs is we face inconceivable existential crises, climate change and income inequality. CEOs need to understand stewardship, which means creating economic value by integrating needs of multiple stakeholders, society, future generations and environment. Today, we must create superior shareholder returns by addressing humanity's challenges. WEF state this is $10.1 trillion annually in new business opportunities, addressing climate change and income inequality.

Boards must find CEOs who are steward leaders, the genuine desire and persistence to create collective better futures for multiple stakeholders and future generations. They must believe in interdependence regarding successes. Those who don't understand this shouldn't be CEOs. COVID taught us no-one is safe until everyone is safe. Steward leaders creating ESG and sustainability excellence believe in four values: interdependence, long-term view, ownership mentality and creative resilience, and based on these, give their organisation stewardship purpose, collective better futures. When the values and purpose are developed, everything from board to management is viewed through the steward leadership compass. Look for steward leaders for CEO succession, the world needs it, alongside technical skills and willingness.

Nga Pham:
What are best practices for transitioning to new CEOs?

Yuelin Yang:
I'm close to some A.P. Moller employees, particularly the Asian and Singapore Head. In its sixth generation, they've only had two non-family CEOs. The new Chairman is 40-something. My friend in Singapore is Family Advisor and they want to provide steward long-term family shareholding to help CEO succession. One person they selected was an external candidate, but they provide a family shareholder as a long-term base.

Roland Bosch:
What can companies do for investors to better assess softer skills, and regarding proxy voting, exceed numbers of independent board members or one female board member?

Christine Chow:
It takes time and must be gradual through multiple years. There's no perfect way, but well documented knowledge build-up with Asset Managers or owners usually helps.

Rajeev Peshawaria:
Boards must understand companies' intangible value. 65-85% of stock market valuation in some industries is intangibles, e.g., leadership quality, strength of culture, innovation ability. Boards can evaluate these by understanding if brains, bones or nerves are unhealthy, the employees see it first. A seven-minute survey asking employees about health should be done once a year.

Christine Chow:
Glassdoor?

Rajeev Peshawaria:
There are instruments for building cultures based on steward leadership, e.g., the Steward Leadership Quotient, if employees feel empowered to live ESG, sustainability and stewardship. Boards must better assess intangibles and invest more time on discussions.

Rebecca Treadway:
What should companies do to retain board members amidst M&A and changing dynamics, technology, leadership and strategy?

Jaeuk Khil:
In Korea board member tenure is limited by law to six years. Using company resources with soft skills reveals good characteristics. We must choose between retaining independence or good members.

Rajeev Peshawaria:
In ASEAN countries board members tend to remain indefinitely. There shouldn't be age discrimination. Some 95-year-olds are very sharp. Directors must stay up-to-date and understand changing industry and global dynamics, stay sharp, to remain on boards. Assess only their board contribution.

Luz Rodriguez:
Institutional investors must continually demand high-quality board members and CEOs. Corporate governance and proxy voting are our strongest tools.

Christine Chow:
Tang Dynasty 600-900AD, Emperor Tang Taizong, had an Independent Director, Wei Zheng, who continually challenged him. The Emperor threatened to kill him because he could no longer take his truth. His wife, Empress Ma, fell to the floor, saying "Congratulations, Emperor. I heard, historically, only the best Emperor would have someone who tells him the truth. I want to congratulate you." Family governance is never easy, but those who are truthful, with supportive family members, will have successful businesses.

Yuelin Yang:
The gap between concentrated family ownership and dispersed is big. In Asia, certainly in my family, when founders pass away, leaving hundreds of millions to billions of dollars, family members are recruiting Independent Directors to offices. Hong Kong and Singapore are small. My mom was on Bank of China (Hong Kong) board in 2003, with others like Victor Fung, [Xi Xi Tan, Wei Jin Shang – 357:54], all part of Hong Kong's infrastructure. Flying in six to eight times annually, she was the one pounding the table.