
BOARD OF DIRECTORS: STRUCTURE AND CONSEQUENCES

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ABSTRACT

This study examines board diversity as a crucial component of board structure and its role in enhancing board effectiveness and strengthening corporate governance in listed companies. The effectiveness of a board depends not merely upon its size or formal composition, but on an optimum combination of directors possessing diverse skills, knowledge, expertise, experience, independence, gender representation, and decision-making capabilities. The study argues that board diversity contributes significantly to strategic leadership, transparency, accountability, and sound corporate decision-making, which are essential pillars of good corporate governance. Drawing from the principles of stewardship theory, the paper emphasizes that directors act as fiduciaries entrusted with protecting the interests of shareholders and other stakeholders through informed and ethical governance practices.

The research critically analyses the legal and regulatory framework governing board structure and diversity under the Companies Act, 2013 and SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, along with the recommendations of the SEBI Committee on Corporate Governance (Uday Kotak Committee). Particular attention is given to various dimensions of diversity, including board independence, gender diversity, age diversity, and diversity in skills and technological expertise, highlighting how these dimensions contribute to effective governance and improved firm performance. The study further examines the role of board committees, especially the Nomination and Remuneration Committee and the Audit Committee, in identifying competent and diverse directors and ensuring vigilant monitoring and transparency.

An important focus of the study is board evaluation as a governance mechanism for assessing board performance, identifying deficiencies in composition, and promoting continuous improvement. It demonstrates how evaluation processes help in achieving balanced board composition and reinforcing accountability. Adopting a doctrinal methodology based on statutes, reports, books and scholarly writings, the study concludes that a

well-diversified board enhances board effectiveness and acts as a catalyst for robust corporate governance. It further suggests that diversity should not be viewed merely as regulatory compliance, but as a strategic governance tool essential for sustainable growth, responsible management, and long-term value creation in modern corporations.

Keywords: Board Diversity; Board Effectiveness; Corporate Governance; Board Structure; Independent Directors; Gender Diversity; Board Evaluation; SEBI (LODR) Regulations; Companies Act, 2013; Board Committees; Stewardship Theory; Good Governance.

Introduction

The effectiveness of Board depends on many factors, one of which is Board Structure and the key to good Corporate Governance is efficient, informed and well diversified board who understands its role of appreciating the issues put forward to them and honestly trying to discharge its responsibility by providing solution to those issues and in doing so the board uses its inherent weapons of skill, knowledge, experience, decision making ability, risk taking ability etc. This list is not exhaustive. It is pertinent to note that these inherent weapons are contributors to board diversity. It can so happen that a director on Board is skilled but he lacks decision making ability or risk taking ability, so in that case Board should have another person who is good in decision taking or a good entrepreneur in the field required. Board Structure is the foundation for an effective board and effective board is one which provides leadership, strategic guidance and takes quality decisions and while doing so remaining accountable to the shareholders.

Good Corporate Governance enhances transparency, fairness and accountability and these are some of the concerns that Boards deal with. Here the Stewardship Theory comes into picture, because it is the board of directors who are considered as trustworthy people who look after the interest of shareholders. The position of the Board is that of trust that is bestowed with the responsibility to work in the best interest of shareholders and working of the company depends on how well the interest of these stakeholders viz. Shareholders, creditors, banks etc are served. Board evaluation also plays an important role in board effectiveness and in checking whether board diversity has been achieved or not. The Companies Act and SEBI (Listing Obligation and Disclosure Requirement) Regulations, 2015 has provision that require a mechanism to be put in place to conduct performance evaluation of board collectively and directors individually. Thus as a measure for good corporate governance the provisions mandate for a well diversified

board equipped with skills, knowledge, experience and also performance of such directors and board should be evaluated, moreover for good corporate governance it is mandatory to have a code of conduct for directors and employees and such code of conduct shall also relate to non-executive directors including Independent Director. The Code gives guidance and support to directors needed for ethical conduct of business and compliance with the laws. Such Code of conduct is to be put on website as a mandatory compliance with law.

Objectives of the Study

The present has been carried out with the following objective:-

- i To understand the concept of one of the component of board structure i.e. board diversity;
- ii To probe into how board diversity leads to board effectiveness;
- iii To understand the role of board committees and how they contribute to board diversity;
- iv To understand the concept of board evaluation and how board evaluation leads to board diversity.

Significance of the Study

This study undertakes to understand what board structure is; the concept of Board Diversity which is a component of board structure. This study only talks about the listed companies and its compliances with regard to board structure, it also talks about presence of women directors on board, this study explains the significance of board evaluation process and how this evaluation helps in achieving board diversity. This also incorporates the recent recommendations of SEBI committee on corporate governance and how such recommendations are important in achieving board diversity.

Research Questions

The researcher tries to find out the following research questions: -

1. What is Board Structure *vis-a-vis* board diversity?

2. How Board Diversity leads to board effectiveness?
3. How board evaluation helps in achieving board diversity?

Research Methodology

The methodology adopted in this research is Doctrinal. The study is based on the collection of data from secondary sources such as books and internet. The study also involves the collection of data from primary sources such as statutes.

BOARD STRUCTURE *vis-a-vis* DIVERSITY IN THE BOARDROOM

Concept of Board Diversity

The word “Diversity” has not been defined in any Act but diversity in the Board means diversity in thought, experience, skill, understanding, leadership quality, gender diversity etc. Thus diversity is proper balance of executive, non executive, independent, women director, resident, small shareholder director who possess these inherent weapons which help to solve a given challenge. Board Structure is the foundation for an effective board and this effective board is possible with this optimum combination of directors. The inherent weapons when directors use to solve the given issue helps to achieve the board effectiveness which *inter alia* leads to good corporate governance.

Over the years regulators have emphasized on the role of non-executive directors, specially on the role of Independent director and how their presence on Board is crucial for a transparent flow of information to shareholders and also emphasized on the significance of balancing skills and experience of the board members.¹ Thus it can be inferred that diversity means not only having collection of individual who are different from each other but also getting the right people for the job and harnessing their unique quality which will benefit the organisation and the business.

Board Size

The structure of the organisation along with its needs play an important role in determining the

¹ Sathyanarayana Reddy, V Balachandran, “Diversifying the Boards of Directors- A step towards better Corporate Governance”, *Chartered Secretary*, Vol. 46, No. 04, April 2016, pp. 54-59.

size of the Board. It is important to note that less the board size more involvement of directors in meetings which *inter alia* means more the average attendance of the directors, more will be their accountability and more will they function as a team and on the counter part more the board size, less the involvement of directors in the meetings and Judge and Zeithaml (1992) had found that larger board are less involved in strategic decision making and so less the average attendance of such directors, less accountability of the directors and less they function as a team, larger board size usually face problems in reaching a consensus on important decisions. If the size of the board is too small, its members are overloaded and are unproductive and if the size too big than every director may not have chance to participate in some decisions and there is more difficulty in coordination (Gladstein, 1984). Thus there should be optimum size of the Board i.e. neither too small nor too big.²

It is pertinent to note that every Board needs sufficient expertise to accomplish its vision and mission of the organisation, hence perfect combination of directors with proper skill, knowledge, experience, leadership quality plays an important role in achieving such vision and mission.

How large should our Board be in order to achieve board diversity?

Section 149(1) of Companies Act, 2013 states that a minimum number of three directors in the case of a public limited company and two in the case of a private company and maximum fifteen directors. A company may appoint more than fifteen only on passing special resolution.³

In order to enhance the standards of Corporate Governance SEBI formed a committee on corporate governance in June, 2017 under the chairmanship of Mr. Uday Kotak and this committee was asked to submit report on various issues on October 5, 2017.

This committee was of the opinion that board of directors with diverse background do play an important role in enhancement of company's governance system. Hence there should be sufficient number of directors to carry out the organisation's mission. Hence this committee suggested that as there is no provision in SEBI (Listing Obligation and Disclosure

² Jerry Goodstein, Kanak Gautam and Warren Boeker, "The Effects of Board Size and Diversity on Strategic Change", *Strategic Management Journal*, Vol. 15, No. 3, March 1994, pp.242-243

³ *Companies Law Manual, Companies Act 2013 along with Rules*, Taxmann Publications Private Limited, 2015

Requirement) Regulations, 2015, the committee recommends that a listed entity should have minimum of six directors.⁴

Board Diversity, Board Effectiveness and Corporate Governance

Right balance of Independent Director

The Independent Directors belong to a category of directors who are impartial and play a pivotal role in enhancement of good corporate governance. They bring accountability and transparency along with them. It is because of these qualities of impartiality and transparency that their role is increasing day by day. Presence of Independent Directors on board is one of the contributors to board effectiveness which ultimately leads to good corporate governance. Company while selecting an Independent Director shall exercise the necessary due diligence that is required and such persons can be selected from a data bank maintained by any association, body as notified by Central Government. The persons selected should be completely independent from all aspects. After the person is nominated by the board, the appointment of such person requires approval of shareholders in annual general meeting or extra-ordinary general meeting.

Section 149(4) of Companies Act, 2013 provides that at least one third of the total number of directors shall be independent director⁵ and Central Government may prescribe for certain class or classes of public company that it should have minimum two independent directors.⁶

According to Regulation 17 of SEBI (Listing Obligation and Disclosure Requirement) Regulations, 2015, board of directors shall have optimum combination of executive and non-executive directors with at least one women director and not less than fifty percent of the board of directors shall comprise of non-executive directors.⁷

Where Chairman is non executive director than one-third of board shall be independent Director and where chairman is executive at least half shall be independent director and where chairman a promoter or related to a promoter than half of the board shall consist of independent

⁴ SEBI Committee on Corporate Governance, 'Report on Corporate Governance (2017)'.

⁵ *Supra Note 2*

⁶ Rule 4 of Companies (Appointment and Qualification of Directors) Rules, 2014

⁷ SEBI (Listing Obligation and Disclosure Requirement) Regulations, 2015, Regulation 17

director.⁸

Formalities to be complied with⁹:-

- Appointment letter along with full profile of the Independent Director is to be uploaded on the website.
- The code of conduct that is to be uploaded on website shall incorporate duties of independent director as well.
- Schedule IV of Companies Act, 2013 requires that at least one meeting in a financial year in which only independent directors are to be present i.e. non presence of non independent directors or members of management.
- Regulation 46 details of familiarization programmes imparted to independent director including number of programmes attended and number of hours spent in such programmes.

Gender Diversity

Our constitution enshrines that there should be no inequality and predominately this inequality exists between human beings on the basis of sex. Human Beings fail to treat other human beings at par, and gender inequality is most common and unavoidable. This gender inequality can be seen at work place also. To remove this gender inequality on board, legislature has taken bold step by making it mandatory for the companies to appoint women director on board and has taken action against those companies who have not complied with the provisions.

Moreover many countries across globe have shown participation of woman directors on board. Countries like Belgium, France, Germany, Austria, Italy, Spain etc have shown that because of woman participation on board there has been increase in the income of Companies.¹⁰

⁸ *Supra Note 6*

⁹ Rajesh Arora, Sona Rajora, “Comparative Analysis of the Listing Agreement and Chapters III & IV of SEBI(Listing Obligation and Disclosure Requirements) Regulations, 2015”, *Chartered Secretary*, Vol.46, No. 02, February 2016, pp.32.

¹⁰ Prashanti Upadhyay, “A Critical Analysis of Need For Women Directors in Indian Companies”, available at <http://www.manupatrafast.in/Articles/PopOpenArticle.aspx?ID=820fc25f-043a-422f-9829-2271d481d06f&txtsearch=Text%20Search:%20women%20director>.

Well diversified board do play an important role in achieving the mission of the organisation. Well diversified board consist of well skilled, knowledgeable, experienced board and one among it is gender diversity which is seen to play an important role in decision making. The Companies Act and SEBI (Listing Obligation and Disclosure Requirement) Regulations, 2015, have already taken steps to make it mandatory for the Companies to have a woman director on the board. SEBI was strict about the mandatory appointment of women director hence it also imposed huge penalty for non compliance and further warned to take action against the promoters and directors if the said compliance was not met.

It is seen that the decision making by the women on board provide better financial returns than those without. “An analysis of return on equity (ROE) data of top 100 Indian companies (BSE 100) by Randstad, a leading HR services provider, says that companies with women on their boards have a positive impact on ROE. ICICI Bank, headed by Chandra Kochhar, has shown a positive difference on return on equity”¹¹

As per the recent recommendation of SEBI committee formed on Corporate Governance, the presence of women director has a positive impact on decision making process and such their recommendation is to improve the board effectiveness by including women independent director. If we look at many companies we see that women directors who are appointed are usually members of their own family (wife, sister or daughter), thereby complying with the provisions of the Act and Regulations. The true essence for which it was made mandatory to appoint a women director was missing. Thus the recent recommendation is in the line of this true essence which requires one women independent director to be appointed on board. If this recommendation is implemented than the structure of the board of many companies will again have to be changed. Thus this recommendation if implemented will surely lead to unbiased decision on board by the person who is known of her decision making quality.

Age Diversity

Well diversified board also includes age diversity, but this criterion is generally overlooked. Age Diversity includes in its ambit people of all age. Directors who are in their sixties are believed to have experience and knowledge and hence they have their own place in the boardroom and at the same time board requires young dynamic directors who can take

¹¹ S. Mukherjee, N. Singh “Company with Women Board Members make more money”, *Times of India*, 27 October 2014

decisions or have the leadership quality. Thus Diversity in board includes age diversity also so that there remains proper balance of skills.

According to Companies Act, 2013 a person may be appointed or continue as a directors if he has attained the age of seventy years only after passing of special resolution but till now no specific provision for non- executive directors have been laid down.

SEBI (Listing Obligation and Disclosure Requirement) Regulations, 2015 has not prescribed any age limit for directors especially for non executive directors. Hence SEBI committee in its recent report recommended that no listed entity shall appoint or continue the appointment of a person as a non executive director who has attained the age of seventy five years except on passing special resolution. For appointing a person with special resolution a notice along with explanatory statement stating the reasons for such appointment shall be mentioned. It is pertinent to note that though age cannot be the criteria for disqualification of a non -executive director but by looking at the role and significant commitment which it requires the committee was of the opinion that there should be certain checks and balances and hence they have recommended such a provision.

Skills, expertise and experience and IT governance

Corporate Governance means set of responsibilities that are discharged by the board and executive management with the aim of providing direction to achieve the mission of the organisation and this mission is achieved by identifying the risks and taking steps to mitigate the risks. These risks can be identified with the help of technology and this inescapable use of technology has created dependency on Information Technology and that calls for focus on IT governance.

IT being the backbone for any business is no longer a separate entity but is an essential part of the enterprise and in order to achieve the mission of the enterprise it is important to use technology to identify the venues where it can invest. Skill, expertise and experience are the foremost requirements for any board to be effective and IT governance is the duty of the board and executive management. IT governance is important because it helps in decision making process; it delivers value to the organisation and helps to mitigate risks. In order to appropriately discharge its IT function board should have insight of IT environment and thus

it also needs appropriate skills on board in this regard. Hence than the diversified board plays an important role.¹²

In Companies Act and SEBI (LODR) 2015 there is no specific requirement of disclosure of skill and expertise. It is only for Independent Director that his profile has to be uploaded along with appointment letter on website and this requirement is not for any other director. In today's world it is important that board possesses such skills, knowledge and expertise and also important that these skills, knowledge and expertise should also be known to the shareholders for whom directors carry out the functions. It is the shareholders who are considered as principal and so it is their right to know about the skills, knowledge, experience about the directors who work for them.

According to the recent recommendation of the SEBI committee on Corporate Governance, the committee also focused on the disclosure of expertise/ skills of directors and thereby acknowledged that though the board may take external advice from an expert on a particular issue but the need for the board to make informed business judgement and for that informed judgement decision the board should be well diversified i.e. should comprise of technical/ academic skill, general management, etc. In order to bring transparency the SEBI committee on corporate governance recommended to the board of directors of every listed company should possess the required list of competence which the company believes its directors to possess. Such disclosure has to be made in the corporate governance section of the annual report. Such Disclosure shall include the list of core skills/ expertise/ competence as required by the board of directors and the names of directors who possess such requirements.

Role of Board Committees in achieving Board Diversity

Nomination and Remuneration Committee

Section 178 of Companies Act, 2013 lays down that every listed company shall constitute a Nomination and Remuneration committee which shall consist of three or more non-executive directors out of which not less than one half shall be independent directors. Provided that chairman (whether executive or non-executive) of the company can be appointed as the

¹² Tapas Bhattacharya, "Role of Information Technology in Corporate Governance", *Chartered Secretary*, Vol. 46, No. 02, February 2016, pp.48-51

member of the committee but he cannot chair such committee.¹³

Regulation 19(1) of SEBI (Listing Obligation and Disclosure Requirement) Regulations, 2015 states that the board of directors shall constitute the nomination and remuneration committee which shall consist of: -

- At least three directors;
- All directors shall be non- executive;
- At least fifty percent shall be independent directors.

The role of the committee is stated in Part D of Schedule II which lays down following: -

- Formulate criteria for determining qualification, positive attributes and independence.
- Formulate criteria for evaluation of the performance of directors.
- Identify persons capable of becoming directors.
- It is also the duty of the committee to decide whether to extend the duration of independent director or not and such decision is based on evaluation report on performance of the director.

Nomination and Remuneration committee do play an important role in identifying people with diverse background. It is the responsibility of this committee to identify persons who are qualified to become directors, it should lay down the criteria for determining qualifications, positive attributes and independence of director, should also identify persons with different experience, skill, knowledge, persons who are capable of decision making, who can take risks. Thus the Nomination and Remuneration committee has to be diligent enough in identifying persons with the above qualities.

Audit Committee

Section 177 of Companies Act, 2013 provides that the Board of listed company shall constitute an audit committee which shall consist of minimum three directors with independent directors

¹³ *Companies Law Manual, Companies Act 2013 along with Rules*, Taxmann Publications Private Limited, 2015

forming the majority. It is also provided that the majority of the members of Audit Committee including the Chairman should be persons with the ability to read and understand the financial statements.

According to Regulation 18 of SEBI (Listing Obligation and Disclosure Requirement) Regulations, 2015 every listed company shall constitute an audit committee which shall consist of minimum three directors, two- third being independent directors and all members shall be financially literate and at least one should be accounting or financial management expertise.

If we look at the composition of the Audit Committee it can be said that there should be members who are literate and financial literacy means who can understand financial statements, thus the above requirements can only be achieved if Nomination and Remuneration committee is vigilant enough in choosing the members of the board and formulates the criteria for board diversity. Thus board should include persons who understand financial statements as well along with other requirements.

Now we will see how the audit committee contribute to corporate governance.

Vigilant Monitoring and Independent Director

The Shareholders act as principals and want managers to work in their best interest i.e. to maximise the wealth of shareholders, but managers sometimes due to their selfish motive try to maximize their own wealth and least care about the shareholders. These problems are usually seen in large organisations.

The role of audit committee is to act independently and vigilantly. Here the role played by independent director is important because they are the majority composition of audit committee. Function of the audit committee is to meet the external and internal auditors to review the financial statements, audit process and internal accounting. This helps to solve agency problems, by timely releasing the unbiased accounting information to the shareholders, creditors.¹⁴

¹⁴ April Klein, "Firm Performance and Board Committee Structure", *Journal of Law and Economics*, Vol. 41, 1998, pp. 275-304.

This monitoring by audit committee helps in day-to-day increase of firm performance, thus it can be said that this increase in firm performance is due to the outside directors sitting on audit committee and nomination and remuneration committee.

Thus we see that how the presence of independent director increase the informational transparency of the company and this presence of independent director is due to diversity on board and provisions of the companies act and SEBI regulations helps to achieve such board diversity.

Board Evaluation and Board Diversity

Section 134 of The Companies Act, 2013 states that boards report shall contain a statement indicating the manner in which board evaluation has been made by the board of its own performance, of committees and individual directors.

The nomination and remuneration committee shall carry out the evaluation of director's performance and independent director shall give an objective view in the evaluation of the performance. Independent director shall be re-appointed only on the basis of report on evaluation and this evaluation is to be carried out by the board of directors except by the directors whose performance is being evaluated.

Board Evaluation is an important tool to access the level of board effectiveness. It is because of board evaluation that helps the board confirm whether diversity of the board has been achieved or not i.e. whether suitable balance of skill/ knowledge/ experience/ gender diversity has been achieved or not. Board Evaluation also helps the board to focus on any inadequacies, to review its practices and procedures, and it is only after board evaluation that a director is re-appointed. While doing board evaluation it is important that evaluation should answer following questions:

- How do directors work as a team;
- Is there proper balance of skill, knowledge, experience i.e. is the board well diversified;
- The decisions taken by the board are within the applicable laws and regulations; As per the recent recommendation of SEBI committee the listed entity shall at least once every year, undertake a formal updating programme whereby which the board of directors

will be updated with the recent changes in law i.e. the various compliances with the laws.

- Do the decisions of the Board take into account the shareholders views;
- Is the composition of the board being refreshed;
- How effective is the lead Independent Director;
- The level of commitment of each board member, do they properly use their inherent skills and work towards achieving the organisation's mission;
- Are there any unmanaged conflict of interest;
- Is the board really independent?

It is pertinent to note that non-executive directors do play an important role in achieving board effectiveness and this can only happen if there is proper interaction between non-executive director and senior management. It is the duty of chairman and other board members should consider and evaluate how well are the non-executive director informed about the company, how well are they prepared for the board meetings, and are they meeting the attendance criteria led down by Act and Regulations; Do they devote the necessary time and participate the events outside the boardroom.

In the context of the above statement even the SEBI committee have expressed their views and recommended that the listed entity shall at least once every year undertake a formal interaction between non-executive directors and the senior management. This interaction will help the non-executive directors to understand the company's business. Currently there is no such provision which helps in such interaction between both non-executive director and senior management.

The performance of board committee is also very important for board effectiveness. While evaluating following should be adhered to: -

- How effective is the board committee?
- Does the board committee put important matters before the board to take note of the

same?

- Are the committees acting independently?
- Is the committee proper mix of individuals with skill/ knowledge/ experience etc?

If the board evaluation is carried out properly than surely it will lead to board effectiveness.¹⁵

SUGGESTIONS AND CONCLUSION

In this study an attempt was made to understand the board structure through board diversity and how various components on board diversity i.e. board independence, gender diversity, age diversity, skill, knowledge, experience play an important role in board effectiveness. This board effectiveness *inter alia* leads to good corporate governance. Good Corporate Governance enhances transparency, fairness and accountability and these are some of the concerns that Boards deal with.

It can be inferred from this study that board independence is the utmost requirement of board and hence the role of Independent director comes into picture. Independent Directors are directors who are impartial and play a pivotal role in enhancement of good corporate governance. They bring accountability and transparency along with them. It is because of these qualities of impartiality and transparency that their role is increasing day by day.

Gender diversity introduces the importance of women director on board and this importance has already been recognised by Companies Act and SEBI Regulations, but to make it more stringent the SEBI committee has come up with the women independent director so that women can actually exercise the role of decision making in enhancing corporate governance. If this recommendation is implemented than the structure of most of the companies will be changing.

The knowledge with experience do play an important role, hence the experienced people on board can contribute towards good and sound decision making process, thus age diversity also plays an important role in board effectiveness. We are well aware of the fact that how technology development is taking place. Technology has become the backbone for any business and is no longer a separate entity but an essential part of the enterprise and in order to

¹⁵ Komal Patwari, "Performance Evaluation of Board", *Chartered Secretary*, Vol. 46, No. 05, May 2016, pp. 52-56.

achieve the mission of the enterprise it is important to use technology to identify the venues where it can invest. It is also helpful in identifying risks and thus this dependency on technology also requires well competent people to understand its use and to take benefit from it. Hence directors with good knowledge of information technology can prove boon to the organisation.

So balance of skill, knowledge, and experience i.e. well diversified board do play an important role in enhancing the effectiveness of board and thereby contributing towards good corporate governance.