

*When things go wrong, as they sometimes will,
When the road you're trudging seems all uphill,*

*.....
When care is pressing you down a bit,
Rest if you must, but don't you quit.*

Try telling that to Independent Directors who are under the glare of increasing scrutiny, and are getting to grips with the fact that what they get to know could be much less than what they ought to know. Is the institution of Independent Director under threat? Are systemic solutions overdue?

Editor

ALARM BELLS OR A WAKE-UP CALL?



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The universe of Independent Directors is grappling with the implication of the orders passed by the Hon'ble Supreme Court of India in the case of Jaiprakash Associates Limited (JAL).

On 11.09.2017, the Hon'ble Supreme Court of India, in a writ petition filed by Chitra Sharma and others against the Union of India and others, directed, inter alia, that "the Managing Director and the Directors of Jaypee Infratech Limited (JIL) and JAL shall not leave India without the prior permission of the Court. Any person who was a Director or Managing Director of JIL or JAL on the date of the institution of the insolvency proceedings against JIL, as well as the present Directors/ Managing Director shall also not leave the country without prior permission of the Court. The foregoing restraint shall not apply to Nominee Directors of lending institutions (IDBI/ICICI/ SBI)".

On 22.11.2017, the Hon'ble Supreme Court of India further directed, inter alia that "neither the Independent Directors nor the Promoter Directors shall alienate their personal properties or assets in any manner, and if they do so, they will not only be liable for criminal prosecution but contempt of the Court." The Court also directed that "the properties and assets of their immediate and dependent family members should also not be transferred in any manner, whatsoever."

While listing the matter to be heard on 10.01.2018, the Hon'ble Court also directed that on that day, all the Independent Directors and Promoter Directors of JAL shall remain present.

The question uppermost in the minds of Independent Directors is whether their non-executive status should lead to their being visited with the same liabilities and consequences as Promoter Directors. Heightening their insecurity is the fact of their being clubbed with Promoter Directors, while Nominee Directors have not been subjected to similar restraints.

The Companies Act, 2013 (the Act) provides a differential treatment to Independent Directors and Non-Executive Directors who are not Promoters or Key Managerial Personnel. Section 149(12) of the Act states that such a Director shall be held liable, only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable through Board processes, and with his consent or connivance or where he had not acted diligently. Simply stated, the statute would seem to hold Independent Directors liable only for what they get to know through Board processes or where they had not acted diligently.

It is beyond the province of this article to speculate on whether the Independent Directors of JAL, the holding company, had, through Board process, information regarding the alleged irregularities of the subsidiary company, JIL, in not providing houses to persons who had made payments therefor. Suffice it to say that if relevant

information had travelled to the Board, or if there was lack of due diligence, the Independent Directors will find it hard to escape liability.

The orders passed by the Hon'ble Supreme Court of India afford an opportunity to revisit the responsibilities and liabilities of Independent Directors. The institution of Independent Directors was first recognized in India through Clause 49 of the Listing Agreement. With the coming into force of the Companies Act, 2013, the institution of Independent Directors now has a statutory basis. This institution is seen as the instrumentality which, among other things, seeks to protect the interest of minority shareholders and other stakeholders.

Schedule IV of the Act, which contains a long laundry list of dos and don'ts, is intended as a guide to professional conduct of Independent Directors to ensure that the confidence of the investment community, particularly minority shareholders, regulators and companies, in the institution of Independent Directors is promoted.

Even prior to the passing of the above cited orders by the Hon'ble Supreme Court, Independent Directors had started to exit Boards owing to what was perceived as the high risk associated with the position, with meagre compensation. Therefore, it is possible to conclude that subsequent to the instant directions, only the very brave or the foolhardy would accept the position of Independent Director on Boards. Should a significant exodus take place, the regulator or lawmaker will be left with one less effective instrument to bring a balance to boardroom discussions and decisions. It is therefore necessary to consider what Independent Directors should do to protect themselves, while adding value to the Boards on which they sit.

Committing quality time to Boards and Committees is a non-negotiable requirement. Constructive engagement with managements, within and outside of, boardrooms is a threshold condition for an effective Independent Director. Asking the right questions and getting the minutes to correctly reflect the discussions and decisions is an absolute must. Where an illegality or an irregularity is observed, or even suspected, the pushback must be strong and effective. Shying away from recording a dissent, when it is merited, can cause considerable damage.

The lawmakers on their part, should recognize that Independent Directors must be provided legitimate protection. One possible safeguard could be a screening mechanism on the lines of the Advisory Board for Bank Frauds, where eminent and experienced persons, carefully chosen, go into the acts or omissions of Independent Directors, before the latter are thrown to the wolves. Failing this, Independent Directors could, sooner rather than later, become an extinct species.

Remember the baby and the bathwater!

Do let us know of any specific issues you would like to see addressed in subsequent issues.

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