

Companies Act 2013

Changes and new requirements impacting Directors

February 14, 2014



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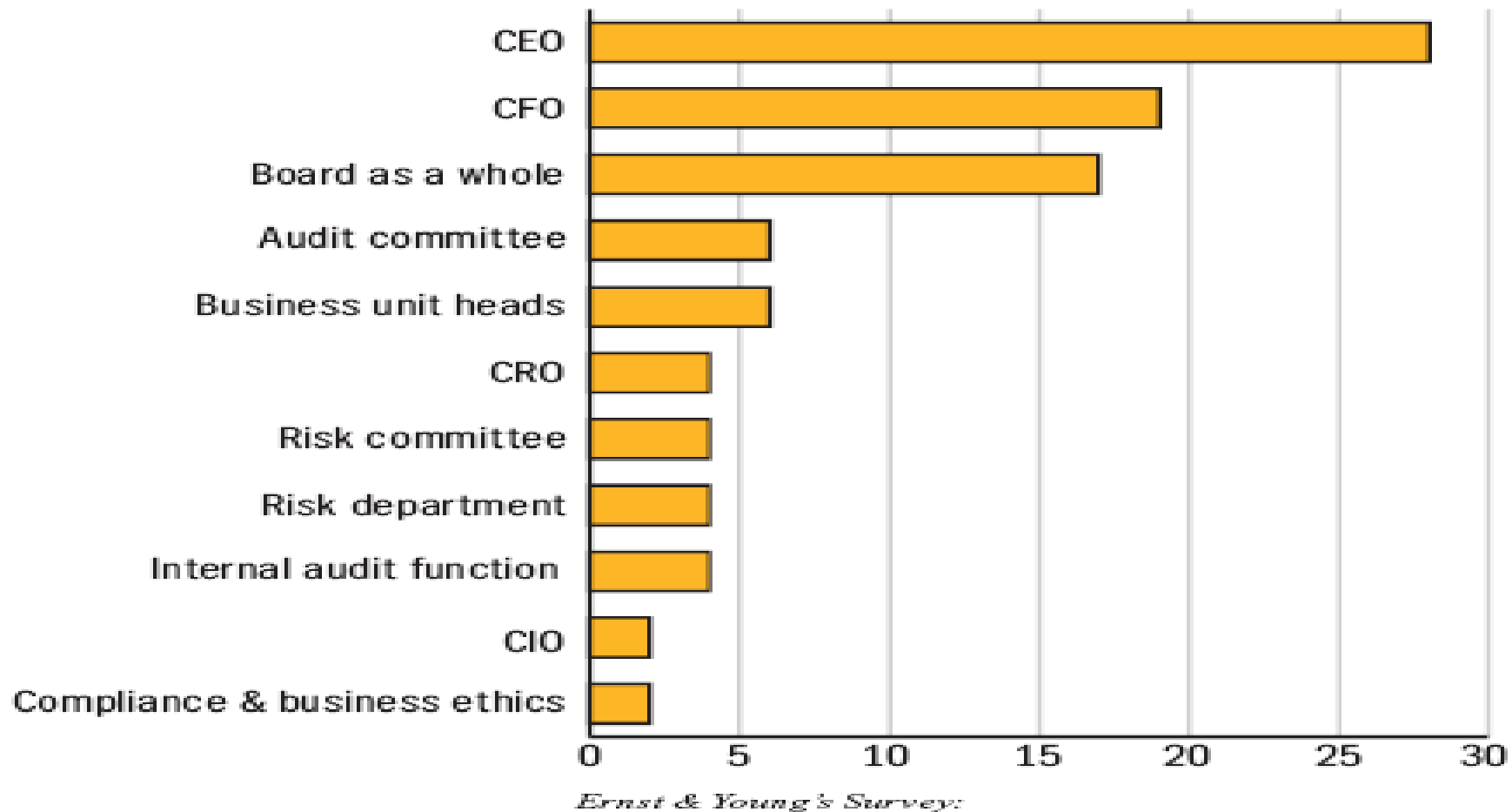
Introductory video



Barings Bank (1762 – 1995)



... so who do you think is accountable?


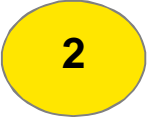
... most people think of the CEO, CFO and Board of Directors





Key changes and new requirements in Companies Act 2013

Directors & Independent Directors: Key changes and new requirements (1/4)

-   **Women director:**
Company should appoint at least one woman director on the Board for such class or classes of companies as may be prescribed. A transitional period of one year has been prescribed to companies for compliance with this requirement

-   **Domicile of director:**
Company should have at least one director who has stayed in India for a total period of not less than hundred and eighty two days in the previous calendar year

-  **Maximum number of directors:**
Company can have a maximum of fifteen directors on the 'Board' and will be applicable to all companies. Any further increase in number of directors, the company will need to pass a special resolution at its 'General Meeting' and no approval from the Central Government is required

-  **Cap on directorship:**
A person will be able to become director in only 20 companies. However, out of this, not more than 10 companies can be public companies

Directors & Independent Directors: Key changes and new requirements (2/4)

5

Composition:

At least 1/3rd of the total number of directors will be independent directors. If higher number has been prescribed under any other governing law/regulation then such company shall comply with the same

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Applicability – Independent directors:

Listed companies or public company having:

- ▶ Paid-up-capital of INR. 100 cr. or more,
 - ▶ Turnover of INR. 300 cr. rupees or more,
 - ▶ In aggregate, outstanding loans or borrowings or debentures or deposits, exceeding INR. 200 cr.
-

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Rotation:



The independent director will be appointed for a period of five years and be eligible for reappointment subject to certain conditions for two terms. Thereafter, the independent director shall be eligible for reappointment after a cooling period of three years



8


Qualification:



Majority of the audit committee members including its chairperson will have an ability to read and understand the financial statements

Directors & Independent Directors: Key changes and new requirements (3/4)



-   **Manner of selection:**
Independent directors to be selected from a data bank maintained by a body, institute association, as may be notified by the central government

-   **Nominee director:**
Nominee directors appointed to the board by financial institutions/investors shall not be considered as independent directors



-  **Relationship with external firms:**
A person is prohibited to be appointed as an independent director, if the person or his/her relative is/was a partner/ executive in an external audit firm, internal audit firm, legal firm and/or consulting firm(s), which have association with the company

-   **Stock options:**
An independent director will not be entitled to any stock options in the company. The Act is not clear as to how a company will deal with stock options granted in the past and which are outstanding at the date of its enactment

Directors & Independent Directors: Key changes and new requirements (4/4)

  **Code for independent directors (Schedule IV):**

Schedule IV sets out a code of conduct for the role, responsibilities and functions of the independent director. Key requirements include need for independent directors to hold at least one meeting in a year to review performance of non-independent directors and framing an evaluation mechanism to evaluate performance of each independent director

  **Protection for independent directors:**

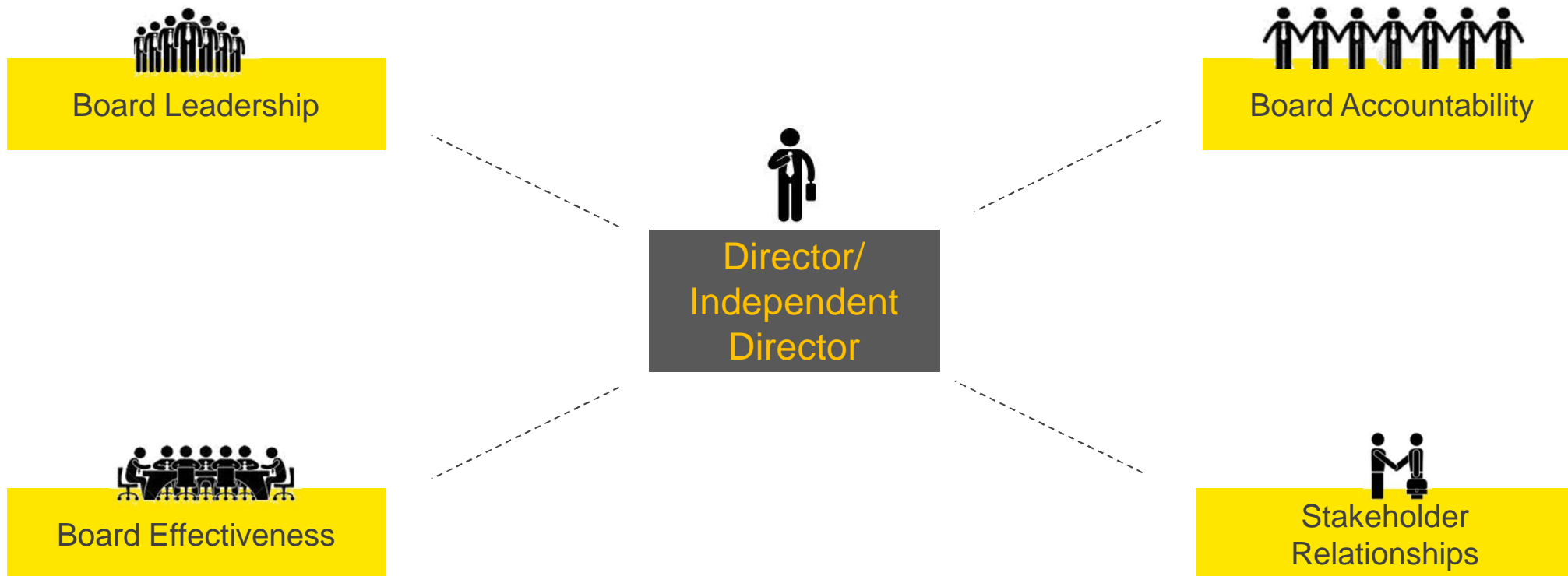
Independent directors shall be held liable, only for such acts by a company which had occurred with their knowledge, attributable through board processes and with their consent or connivance or where they have not acted diligently

Analysis of key changes

- ▶ Listing agreement may be amended to bring it inline with the 2013 Act. In case of any conflict, stricter of the two is expected to apply
- ▶ Listed companies have to revisit the appointment of independent directors. The time frame during which data bank has to be prepared has not been defined
- ▶ Mandatory rotation period is a significant change and is aimed to improve objectivity of the independent director. The availability of qualified personnel to act as independent director could pose challenges in its implementation
- ▶ No clarity provided for stock options granted in the past and remaining outstanding at the date of enactment
- ▶ Most of the attributes listed in the code of conduct for independent directors are qualitative in nature and it may not be possible to demonstrate compliance
- ▶ Class action suit provide empowerment to minority stakeholders to come together and seek action against management, advisors and auditors of the company for mismanagement. The new risks and liabilities will definitely enforce more responsibility into the role of a director

Translating the changes in Companies Act 2013 on ground

2013 Act: Role of Directors/Independent Directors



Aligned to “Comply or Explain” approach being used in mature markets

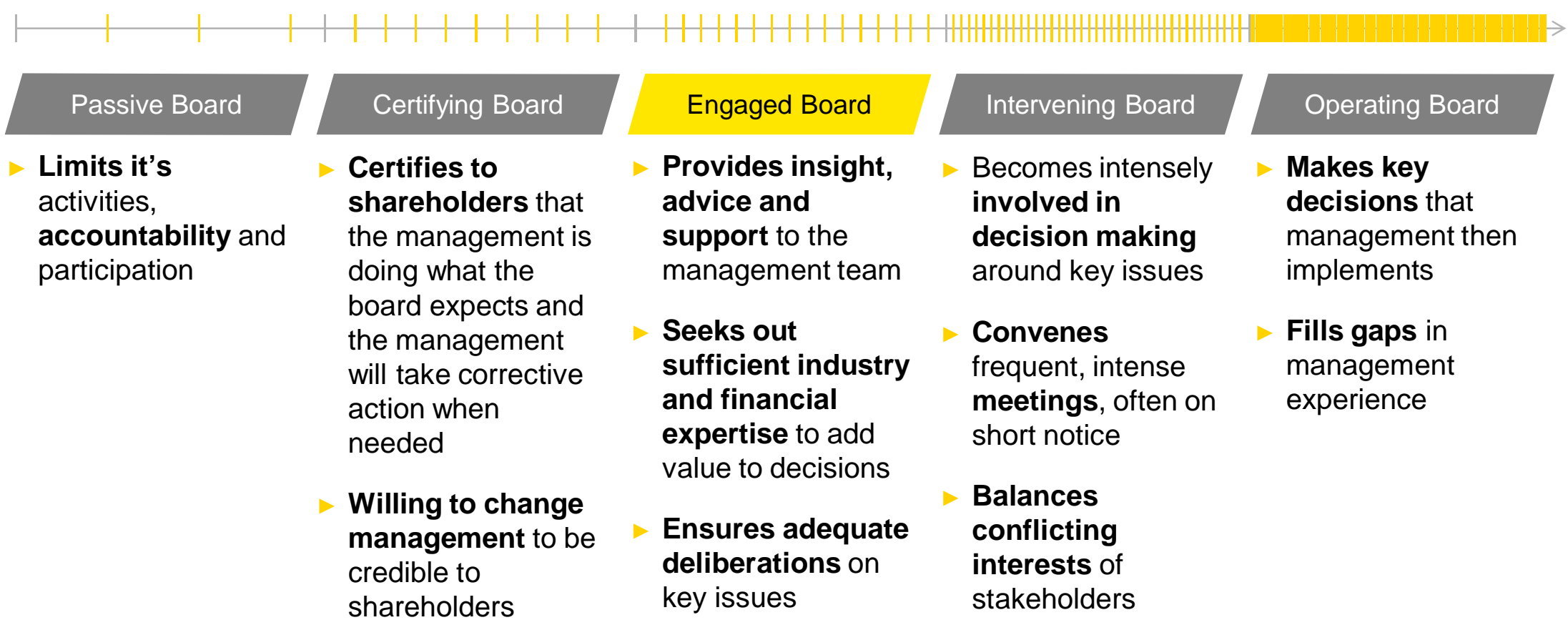
Questions to consider

- 1 Where is my company's Board on a continuum to comply with Schedule IV?
- 2 What and who can I rely upon for ensuring effective compliance with the new provisions?
- 3 How much time is needed as an Independent Director to fulfil my responsibilities?
- 4 How do I balance my fiduciary responsibilities?

1. Board engagement continuum – where are we?

Least Involved

Most Involved



Framework adapted from Harvard Business School


Companies Act 2013 - Expectations of a Board?

1. Board engagement continuum – self assessment

Focus area as per the new Companies Act	Current Engagement	Desired Engagement
Financial Management <ul style="list-style-type: none"> ▶ Internal financial controls ▶ Policies and procedures ▶ Financial reporting ▶ Audit 		
Risk Management <ul style="list-style-type: none"> ▶ Enterprise risk management ▶ Fraud risk & vigil mechanism 		
Corporate Governance <ul style="list-style-type: none"> ▶ Board effectiveness ▶ Board & Director performance ▶ Selection - Directors/KMP 		
External relations <ul style="list-style-type: none"> ▶ Conflict management - related party transactions ▶ Compliance ▶ Corporate Social Responsibility 		
Management Performance <ul style="list-style-type: none"> ▶ Performance assessment ▶ Code of conduct 		
Human Resources and Organization <ul style="list-style-type: none"> ▶ Remuneration ▶ Corporate culture 		

2. What & who can I rely upon?

1st line of defence

- 
- ▶ Identified Key Management Personnel
 - ▶ Senior management and functional heads

2nd line of defence

- 
- ▶ Company Secretary
 - ▶ Auditors: Secretarial
External, Internal, Cost
 - ▶ Advisors / consultants

3rd line of defence

- 
- ▶ Executive Board members
 - ▶ Board Committees
 - ▶ Office of the Board / Audit Committee

3. Where should I spend my time?



Selection & performance assessment

- ▶ Key managerial personnel
- ▶ Senior management
- ▶ Executive directors
 - ▶ Self Assessment
 - ▶ Committee performance
 - ▶ Board performance



Board & other meetings

- ▶ Strategy & planning
- ▶ Committee meetings & consultations
- ▶ Board meetings
- ▶ Shareholder meetings
- ▶ Special meetings



Provide insights, advice and support

- ▶ Financial management
- ▶ Compliance
- ▶ CSR
- ▶ Stakeholder engagement & conflict management
- ▶ Risk management
- ▶ Strategic direction
- ▶ Board effectiveness

4. How do I balance my fiduciary responsibilities?

Obligations & expectations as an Independent Director

- ▶ Independent judgment on Board's deliberations
- ▶ Safeguarding interests of stakeholders
- ▶ Moderating and arbitrating in situations of conflict
- ▶ Ensuring integrity of financial information



How do I balance and safeguard my fiduciary responsibilities?

Wider duties and responsibilities as part of the Board

- ▶ Exercising duties with reasonable care, skill & diligence
- ▶ Not attempting to achieve any undue gain
- ▶ Participating constructively and actively in Board and Committee meetings
- ▶ Keeping well informed about the company and external environment

1 My contract with the Company



2 Director's and officers insurance



3 Effective minutes



Key takeaways...

- 1 Don't get caught in the minutia – remember and actively consider the four broad themes
- 2 Ultimately effective board governance is all about implementation and adhering in true spirit

Q&A



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