Dissecting the New Law

Fulfilling the Criteria for Independence

Independent Directors as per the Companies Bill 2013

Key Governance Issue

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Independence of the Independent Director

Meeting the tough Criteria for Independence for Listed Companies

1. The Companies Bill, 2013 has for the first time defined the term **"Independent Director"** which was previously defined as per Clause 49 of the Listing Agreement.

2. **The Companies Bill, 2013 states that:**

*Every **listed public company** shall have at least one-third of the total number of directors as Independent directors and the Central Government may prescribe the minimum number of independent directors in case of any class or classes of public companies.(Clause 149(4))*

Now let us look at the definition of a "Listed Company":

*"listed company" means a company which has **any of its securities** listed on any recognized stock exchange (Clause 2(52))*

As per my understanding this means if a company has listed its securities apart from equity shares (its debt securities, debentures etc.) it will be treated as a Listed Company and hence it will also have to appoint Independent Directors.

3. However the provisions containing the criteria of "Independence" are creating a major impact in the Corporate Board Rooms these days. Under the Bill both the liability of such independent Directors has been increased and the criteria for Independence has been made stiff.

4. The Bill has defined "officer in default" as:
Every director who is aware of any contravention of any provisions by virtue of receipt of any Board proceedings or participating in such proceeding without any objection or given his consent to such contravention

5. This would mean that:

a. If an Independent Director remains a mute spectator at the Board Meeting **and if any contravention takes place he would be held liable.**

or

b. Even if he was **NOT** present at such board meeting where such decision had taken place and he was in receipt of the Minutes of that meeting and he **DID NOT RECORD HIS OBJECTION in the minutes of the subsequent Board Meeting he would be held liable.**

6. Now let us compare the (comparable) existing provisions of the Clause 49 of the Listing Agreement with Companies Bill 2013 :

Sl.	Listing Agreement	Companies Bill	Impact
1	Where the Chairman of the Board is a non-executive director, at least one-third of the Board should comprise of independent directors and in case he is an executive director, at least half of the Board should comprise of independent directors	Every listed public company shall have at least one-third of the total number of directors as Independent directors and the Central Government may prescribe the minimum number of independent directors in case of any class or classes of public companies.	Listing Agreement would prevail
2	Is not related to promoters or persons occupying management positions at the board level or at one level below the board;	An independent director in relation to a company, means a director other than a managing director or a whole-time director or a nominee director,— (b) (i) who is or was not a promoter of the company or its holding, subsidiary or associate company; (ii) who is not related to promoters or directors in the company, its holding, subsidiary or associate company	1. Nominee Director will not be considered an Independent Director. 2. The Independent director should not have any relation with the Associate Company, its Directors & promoters
3	He has not been an executive of the company in the immediately preceding three financial years;	who, neither himself nor any of his relatives— (i) holds or has held the position of a key managerial personnel or is or has been employee of the company or its holding, subsidiary or associate company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed	Apart from the ID himself, his relatives also cannot hold any position in the company, its holding, subsidiary or its associate in previous 3 years
4	He is not a material supplier, service provider or customer or a lessor or lessee of the company, which may affect independence of the	who has or had no pecuniary relationship with the company, its holding, subsidiary or associate company, or their promoters, or directors, during	Very tough criteria prescribed. There should be NO MONETARY TRANSACTION with any

Sl.	Listing Agreement	Companies Bill	Impact
	director;	the two immediately preceding financial years or during the current financial year; None of whose relatives has or had pecuniary relationship or transaction with the company, its holding, subsidiary or associate company, or their promoters, or directors, amounting to two per cent. or more of its gross turnover or total income or fifty lakh rupees or such higher amount as may be prescribed, whichever is lower, during the two immediately preceding financial years or during the current financial year;	of the entities as prescribed in the bill
5	is not a partner or an executive or was not partner or an executive during the preceding three years, of any of the following: a. the statutory audit firm or the internal audit firm that is associated with the company, and b. the legal firm(s) and consulting firm(s) that have a material association with the company.	An Independent Director cannot be an Employee/ Partner/ Proprietor in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed of the: a. Audit Firm, Practising CS / CWA of the Company or its Holding/Subsidiary/Associate Company. b. Legal/Consulting Firm that has or had any transaction with the company or its holding/ subsidiary/ associate company amounting to 10% or more of the gross turnover of such firm.	The Listing Agreement doesn't define the term "material". Companies in India have very well utilized this loophole & many companies have Independent Directors on its Board who are also partners of the companies Solicitors and Advisors. This practice will have to be reviewed
5	is not a substantial shareholder of the company i.e. owning two percent or more of the block of voting shares	holds together with his relatives two per cent. or more of the total voting power of the company	Relative's holdings clubbed with the Independent Director

7. **The Bill defines the Criteria of Independence as per the Checklist reproduced below :**

Clause No.	Criteria
165	Directorship in Public Companies ***not*** exceeding 10
149 (6)	Other than MD/WTD/ Nominee Director
149 (6)(a)	Person in opinion of Board of integrity and possesses relevant expertise and experience
149 (6)(b)(i)	**Who is or was not a:**
	A promoter of the Company
	A promoter of the Holding Company
	A Promoter of the Subsidiary Company
	A Promoter of the Associate Company
149 (6)(b)(ii)	**Who is not related to :**
	The Promoters of the Company
	The Promoters of the Holding Company
	The Promoters of the Subsidiary Company
	The Promoters of the Associate Company
	The Directors of the Company
	The Directors of the Holding Company
	The Directors of the Subsidiary Company
	The Directors of the Associate Company
149 (6)(c)	**Who has no Pecuniary Relationship of the ID with**
	The Company during preceding two financial years/ current FY
	The Holding Company during preceding two financial years/ current FY
	The Subsidiary Companies during preceding two financial years/ current FY
	The Associate Companies during preceding two financial years/ current FY
	The Promoters of the Company during preceding two financial years/ current FY
	The Promoters of the Holding Company during preceding two financial years / current FY
	The Promoters of the Subsidiary Company during preceding two financial years / current FY
	The Promoters of the Associate Company during preceding two financial years / current FY
	The Directors of the Company during preceding two financial years/ current FY
	The Directors of the Holding Company during preceding two financial years / current FY

Clause No.	Criteria
	The Directors of the Subsidiary Company during preceding two financial years / current FY
	The Directors of the Associate Company during preceding two financial years / current FY
149 (6)(d)	**No Pecuniary Relationship/Transaction of the relatives of ID amounting to 2% of Gross Turnover/ Total Income/Rs.50 Lakh with:**
	The Company during preceding two financial years/ current FY
	The Holding Company during preceding two financial years/ current FY
	The Subsidiary Companies during preceding two financial years/ current FY
	The Associate Companies during preceding two financial years/ current FY
	The Promoters of the Company during preceding two financial years/ current FY
	The Promoters of the Holding Company during preceding two financial years / current FY
	The Promoters of the Subsidiary Company during preceding two financial years / current FY
	The Promoters of the Associate Company during preceding two financial years / current FY
	The Directors of the Company during preceding two financial years/ current FY
	The Directors of the Holding Company during preceding two financial years / current FY
	The Directors of the Subsidiary Company during preceding two financial years / current FY
	The Directors of the Associate Company during preceding two financial years / current FY
149 (6)(e)(i)	**Who, neither himself nor any of his relatives holds or has held the position of a KMP/ Employee in any of the 3 FY immediately precceding the FY of the:**
	Company
	Its Holding Company
	Its Subsidiary Companies
	Its Associate Companies
149 (6)(e)(ii)	**Who is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed, of:**
A	***A firm of auditors or company secretaries in practice or cost auditors of:***
	Company
	Its Holding Company
	Its Subsidiary Companies
	Its Associate Companies

Clause No.	Criteria
B	***Any legal or a consulting firm that has or had any transaction amounting to 10% or more of the gross turnover of such firm of the:***
	Company
	Its Holding Company
	Its Subsidiary Companies
	Its Associate Companies
149 (6)(e)(iii)	Does not hold along with his relatives 2% or more Voting power in the Company
149 (6)(e)(iv)	**Who is not a Chief Executive or director, by whatever name called, of any nonprofit organization that receives 25% or more of its receipts from :**
	The Company
	Any of the promoters of the Company
	Any of the Directors of the Company
	Holding Company
	Subsidiary Company
	Associate Company
	Who does not hold more than 2% of voting power in such nonprofit company

All the companies will have to Comply with the above requirements within 1 year from the commencement of this Act.

Disclaimer : This note is based on the research and contains the views of the author on the above subject. The note is intended to initiate sharing of knowledge on Companies Bill, 2013 and cannot be construed to be any professional or legal advice.

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