Committees under Companies Act, 2013.

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INTRODUCTION

With the globalization and the blurring of the borders, the demands on the board have increased tremendously. The regulatory requirements are complex and the onus on the Board is immense. In this scenario the need to delegate oversight of certain areas to a specialist board committee has become imperative. However, it is to be remembered that even though the board delegates some of the responsibilities to a committee, the ultimate responsibility lies with the board.

Committees are a sub-set of the board, deriving their authority from the powers delegated to them by the board. Under section 177 of Companies Act, 2013, Board of Directors may delegate certain matters to the committees set up for the purpose. These committees are usually formed as a means of improving board effectiveness and efficiency in areas where more focused, specialized and technically oriented discussions are required. These committees prepare the groundwork for decision-making and report at the subsequent board meeting.

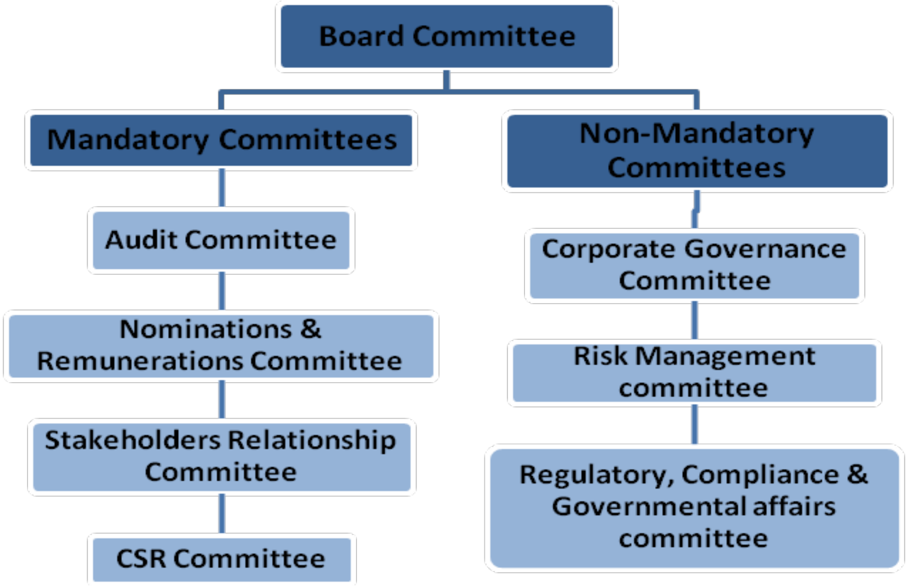
NEED OF COMMITTEES

In the present day, the regulatory requirement is such that the composition of the board comprising executive directors and non-executive independent directors is relatively large in number. In such a situation it becomes at times practically difficult to convene board meetings which suit the convenience and other commitments of each director. By having smaller committees this aspect also gets addressed effectively.

The Board in order to achieve the desired results has to concentrate more with select team members on particular issues. The structure of Board is a key issue for good governance.

VARIOUS COMMITTEES OF THE BOARD

The following are some of the important committees to be constituted by the Board:



MANDATORY COMMITTEES

AUDIT COMMITTEE

A key element in the corporate governance process of any organization is its audit committee. The purpose of constitution of this committee is to make it responsible for the oversight of the quality and integrity of the company's accounting and reporting practices; controls and financial statements; legal and regulatory compliance; the auditors's qualifications and independence; and the performance of company's internal function. The committee functions as liaison between the board of directors and the auditors- external & internal.

Regulatory Framework:

The Regulatory Framework with regard to Audit Committee is covered under:

– Clause 18 of the LODR regulation
– Section 177 of Companies Act, 2013

Section 177 of the Companies Act, 2013 and **Rule 6 and 7** of Companies (Meetings of Board and its Powers) Rules, 2014 deals with the Audit Committee.

Applicability:

The Board of directors of **every listed company** and the following classes of companies, as prescribed **under Rule 6 of Companies (Meetings of Board and its powers) Rules, 2014** shall constitute an Audit Committee.

- all public companies with a paid up capital of Rs.10 Crores or more;
- all public companies having turnover of Rs.100 Crores or more;
- all public companies, having in aggregate, outstanding loans or borrowings or debentures or deposits exceeding Rs.50 Crores or more.

The paid up share capital or turnover or outstanding loans, or borrowings or debentures or deposits, as the case may be, as existing on the date of last audited Financial Statements shall be taken into account for the purposes of this rule.

Composition:

- The Board must have minimum three member out of which at least two/third must be independent directors.
- All the members must be financially literate & one member must be an expert in accounting or related financial management.
- The chairman of the Audit Committee must be an independent director, who must be present at the Annual General Meeting to answer shareholder's query.
- The Company Secretary shall act as the secretary to the committee.

Meeting:

- The Audit Committee should meet at least four times in a year and not more than four months shall elapse between two meetings.
- The quorum shall be either two members or one third of the members of the audit committee whichever is greater, but there should be a minimum of two independent members present.

Functions:

- the recommendation for appointment, remuneration and terms of appointment of auditors of the company;
- review and monitor the auditor's independence and performance, and effectiveness of audit process;
- examination of the financial statement and the auditors' report thereon;
- approval or any subsequent modification of transactions of the company with related parties;
- scrutiny of inter-corporate loans and investments;
- valuation of undertakings or assets of the company, wherever it is necessary;
- evaluation of internal financial controls and risk management systems;
- monitoring the end use of funds raised through public offers and related matters.

Powers:

- To call for the comments of the auditors about internal control systems, the scope of audit, including the observations of the auditors and review of financial statement before their submission to the Board.
- To discuss any related issues with the internal and statutory auditors and the management of the company.
- To investigate any activity within its terms of reference.
- To investigate into any matter in relation to the items or referred to it by the Board.
- To obtain professional advice from external sources.
- To seek information from any employee.
- To have full access to information contained in the records of the company.

- The auditors of a company and the KMP shall have a right to be heard in the meetings of the Audit Committee when it considers the auditor's report but shall not have the right to vote.
- To secure attendance of outsiders with relevant expertise, if it considers necessary.

Review of information:

The Audit Committee shall mandatorily review the following information:

- Management discussion and analysis of financial condition and results of operations;
- Statement of significant related party transactions (as defined by the Audit Committee), submitted by management;
- Management letters / letters of internal control weaknesses issued by the statutory auditors;
- Internal audit reports relating to internal control weaknesses;
- The appointment, removal and terms of remuneration of the Chief internal auditor shall be subject to review by the Audit Committee.

Establishment of Vigil Mechanism:

Every listed company and the companies belonging to the following class or classes shall establish a vigil mechanism for their directors and employees to report genuine concerns or grievances (**Rule 7**):-

a. The companies which accept deposits from the public;
b. The companies which have borrowed money from banks and public financial institutions in excess of fifty crore rupees.

- The companies which are required to constitute an audit committee shall oversee the vigil mechanism through the committee and if any of the members of the committee has a conflict of interest in a given case, they should recuse themselves and the others on the committee would deal with the matter on hand.
- In case of other companies, the Board of directors shall nominate a director to play the role of audit committee for the purpose of vigil mechanism to whom other directors and employees may report their concerns.
- This vigil mechanism shall provide for adequate safeguards against victimization of employees and directors who avail of the vigil mechanism and also provide for direct access to the chairperson of the Audit committee or the director nominated to play the role of audit committee, as the case may be, in exceptional cases.
- In case of repeated frivolous complaints being filed by a director or an employee, the audit committee or the director nominated to play the role of audit committee may take suitable action against the concerned director or employee including reprimand.
- The Vigil Mechanism shall operate for directors and employees to enable them to bring to report genuine concerns. Further the said mechanism shall provide safeguards against victimization and provide for direct access to the chairperson of the Audit Committee in appropriate or exceptional cases.
- *The details of establishment of the Vigil Mechanism is required to be disclosed by the company on its website, if any and in the Board's report.*

Default:

The company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 1 year or with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees or with both.

NOMINATION AND REMUNERATION COMMITTEE

The Nomination and Remuneration Committee set up by the Board is entrusted with combined advisory responsibilities concerning the nomination for appointment, reappointment or dismissal of directors and members of the Executive Committee and the remuneration policies and the individual remuneration of the directors and the members of the Executive Committee.

Regulatory Framework:

The Regulatory Framework with regard to Audit Committee is covered under:

– Clause 19 of the LODR regulation
– Section 178 of Companies Act, 2013

Composition:

- The company shall set up a nomination and remuneration committee which shall comprise at least three directors, all of whom shall be non-executive directors and at least half shall be independent.
- The chairperson of the company may be appointed as member, but shall not chair such committee.
- The Committee shall identify the person qualified to become directors and may be appointed in senior management and recommend their appointment and removal and also carry out evaluation of every director.
- The Committee shall formulate the criteria, for determining qualifications, positive attributes and independence of a director and recommend to the Board the policy relating to remuneration for directors, KMPs and other employees.

Applicability:

1. Every listed Companies; or
2. The following class of companies –
   i) all public companies with a paid up capital of ten crore rupees or more;
   ii) all public companies having turnover of one hundred crore rupees or more;
   iii) all public companies, having in aggregate, outstanding loans or borrowings or debentures or deposits exceeding fifty crore rupees or more.

Meeting:

- The Nomination and Remuneration Committee will meet at least twice per annum and more often if deemed necessary.

- Any director may attend a meeting of the Nomination and Remuneration Committee for the purposes of discussion but is not entitled to vote.
- The Nomination and Remuneration Committee Secretary should attend all meetings to minute proceedings, subject to the discretion of the Committee.

Functions:

- Formulation of the criteria for determining qualifications, positive attributes and independence of a director and recommend to the Board a policy, relating to the remuneration of the directors, key managerial personnel and other employees;
- Formulation of criteria for evaluation of Independent Directors and the Board;
- Devising a policy on Board diversity;
- Identifying persons who are qualified to become directors and who may be appointed in senior management in accordance with the criteria laid down, and recommend to the Board their appointment and removal. The company shall disclose the remuneration policy and the evaluation criteria in its Annual Report.

Default:

The company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 1 year or with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees or with both.

THE STAKEHOLDERS RELATIONSHIP COMMITTEE

Regulatory Framework:

The Regulatory Framework with regard to Audit Committee is covered under:

– Clause 20 of the LODR regulation
– Section 178 of Companies Act, 2013

Composition:

Stakeholders Relationship Committee shall consist of a chairperson who shall be a non-executive director and such other members as may be decided by the Board. The chairperson of the committees or, in his absence, any other member of the committee authorised by him in this behalf is required under the section to attend the general meetings of the company.

Applicability:

Sub-Section(5) of section 178 provides that the Board of Directors of a company which consists of more than one thousand shareholders, debenture-holders, deposit-holders and any other security holders at any time during a financial year shall constitute a Stakeholders Relationship Committee.

Functions:

- The main function of the committee is to consider and resolve the grievances of security holders of the company.
- a committee under the Chairmanship of a non-executive director and such other members as may be decided by the Board of the company shall be formed to specifically look into the redressal of grievances of shareholders, debenture holders and other security holders.
- The grievances of the security holders of the company may include complaints related to transfer of shares, non-receipt of balance sheet, non-receipt of declared dividends, which shall be handled by this committee.
- under the chairmanship of a non-executive director to specifically look into the redressal of shareholder and investors complaints like transfer of shares, non-receipt of balance sheet, non-receipt of declared dividends etc.
- The main function of this committee is to expedite the process of share transfers.

Default:

The company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 1 year or with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees or with both.

CORPORATE SOCIAL RESPONSIBILITY COMMITTEE

The term "Corporate Social Responsibility (CSR)" can be referred as corporate initiative to assess and take responsibility for the company's effects on the environment and impact on social welfare. The term generally applies to companies efforts that go beyond what may be required by regulators or environmental protection groups.

CSR is the process by which an organization thinks about and evolves its relationships with stakeholders for the common good, and demonstrates its commitment in this regard by adoption of appropriate business processes and strategies. Thus CSR is not charity or mere donations. CSR is a way of conducting business, by which corporate entities visibly contribute to the social good. Socially responsible companies do not limit themselves to using resources to engage in activities that increase only their profits. They use CSR to integrate economic, environmental and social objectives with the company's operations and growth.

Applicability:

Sec 135 (1) read with rule 3 of Companies (Corporate Social Responsibility Policy) Rules, 2014, mandates every company (which may include a holding company or a subsidiary company) having:

1. net worth of rupees five hundred crore or more, or;
2. turnover of rupees one thousand crore or more or;
3. a net profit of rupees five crore or more.

During any financial year to constitute a Corporate Social Responsibility (CSR) Committee of the Board.

Any financial year has been clarified as to imply any of the three preceding financial years.

Further a foreign company defined under clause (42) of section 2 of the Act having its branch office or project office in India which fulfils the criteria specified above is required to comply with the provisions of section 135 of the Act and the rules made thereunder. The net worth, turnover or net profit of a foreign Company for the purpose of this section, shall be computed in accordance with balance sheet and profit and loss account of such company in respect of its Indian business operations.

Composition:

Section 135 provides that the CSR committee shall be constituted with three or more directors, out of which at least one director shall be an independent director. Companies (Meetings of Board and Powers) Rules, 2014, however, relax this requirement as below:

- an unlisted public company or a private company covered under sub-section (1) of section 135 which is not required to appoint an independent director, shall have its CSR Committee without such director.
- a private company having only two directors on its Board shall constitute its CSR Committee with two such directors.
- with respect to a foreign company covered under these rules, the CSR Committee shall comprise of at least two persons of which one person shall be as specified under clause (d) of subsection (1) of section 380 of the Act, i.e. the person resident in India authorized to accept on behalf of the company, service of process and any notices or other documents and another person shall be nominated by the foreign company.

The composition of the Corporate Social Responsibility Committee is required to be disclosed in the Board's report prepared under the Act.

Functions & Role:

In accordance with section 135 the functions of the CSR committee include:

- formulating and recommending to the Board, a CSR Policy which shall indicate the activities to be undertaken by the company as specified in Schedule VII;
- recommending the amount of expenditure to be incurred on the CSR activities;
- monitoring the Corporate Social Responsibility Policy of the company from time to time;
- Further the rules provide that the CSR Committee shall institute a transparent monitoring mechanism for implementation of the CSR projects or programs or activities undertaken by the company.

Important Aspects in relation to CSR Policy and CSR Committee:

The Board of Directors of the company shall, after taking into account the recommendations of CSR Committee, approve the CSR Policy for the company and disclose contents of such policy in its report and the same shall be displayed on the company's website, if any.

As per the rules, the CSR Policy of the company shall, inter-alia, include the following, namely –

- a list of CSR projects or programs which a company plans to undertake falling within the purview of the Schedule VII of the Act, specifying modalities of execution of such project or programs and implementation schedules for the same; and
- Monitoring process of such projects or programs. It is to be noted that the CSR activities does not include the activities undertaken in pursuance of normal course of business of a company. The Board of Directors shall ensure that activities included by a company in its CSR Policy are related to the activities included in Schedule VII of the Act.

The CSR Policy of the company shall specify that the surplus arising out of the CSR projects or programs or activities shall not form part of the business profit of a company.

The Board of every company shall ensure that the company spends, in every financial year, *at least two per cent of the average net profits of the company made during the three immediately preceding financial years,* in pursuance of its CSR Policy. CSR expenditure shall include all expenditure including contribution to corpus, the projects or programs relating to CSR activities approved by the Board on the recommendation of its CSR Committee, but does not include any expenditure on any item not in conformity or not in line with activities which fall within the purview of Schedule VII of the Act. Subsection (5) of the section 135, provides that if the company fails to spend such amount of 2%, the Board shall, in its report, specify the reasons for not spending the amount.

Activities covered under schedule VII of The Companies Act 2013:

The activities involve the following:

- Eradicating hunger, poverty and malnutrition, promoting preventive health care and sanitation and making available safe drinking water;
- Promoting education, including special education and employment enhancing vocation skills especially among children, women, elderly, and the differently abled and livelihood enhancement projects;
- Promoting gender equality, empowering women, setting up homes and hostels for women and orphans; setting up old age homes, day care centres and such other facilities for senior citizens and measures for reducing inequalities faced by socially and economically backward groups;
- Ensuring environmental sustainability, ecological balance, protection of flora and fauna, animal welfare, agroforestry, conservation of natural resources and maintaining quality of soil, air and water;
- Protection of national heritage, art and culture including restoration of buildings and sites of historical importance and works of art, setting up public libraries, promotion and development of traditional arts and handicrafts;
- Measures for the benefit of armed forces veterans, war widows and their dependents;
- Training to promote rural sports, nationally recognized sports, paralympic sports and Olympic sports;
- Contributions or funds provided to technology incubators located within academic institution which are approved by the Central Government;
- Rural development projects.

Reporting for CSR:

Rule 8 of the CSR Rules provides that the companies, upon which the CSR Rules are applicable on or after 1st April, 2014 shall be required to incorporate in its Board's report an annual report on CSR containing the following particulars:

- A brief outline of the company's CSR Policy, including overview of projects or programs proposed to be undertaken and a reference to the web-link to the CSR policy and projects or programs;
- The composition of the CSR Committee;
- Average net profit of the company for last three financial years;
- Prescribed CSR Expenditure (2% of the amount of the net profit for the last 3 financial years);
- Details of CSR spent during the financial year;
- In case the company has failed to spend the 2% of the average net profit of the last three financial years, reasons thereof.

<u>If a company ceases to be covered under section 135:</u>

Rule 3(2) of the Corporate Social Responsibility Rules, 2014 provides that every company which ceases to be a company covered under section 135(1) of the Act for three consecutive financial years shall not be required to:

- constitute a CSR Committee ; and
- Comply with the provisions contained in subsection (2) to (5) of the said section till such time it meets the criteria specified in sub section (1) of Section 135.

<u>Effect of None complying with CSR provisions:</u>

If a Company fails to provide or spend such amount, the Board shall specify reasons for not spending the amount in the reports.

Thus, spending on CSR activities is not mandatory and no penalty can be imposed for non-compliance.

NON-MANDATORY COMMITTEES

A company may have as many non-mandatory companies as it would require for efficient oversight of the company. Board of Directors may also constitute other Committees to oversee a specific objective or project. The nomenclature, composition and role of such Committees will vary, depending upon the specific objectives of the company. A few examples of such Committees prevalent in the corporate sector in India and abroad are given below:

CORPORATE GOVERNANCE COMMITTEE

The Corporate Governance Committee is responsible for considering and making recommendations to the Board concerning the appropriate size, functions and needs of the Board. The committee is responsible for considering matters relating to corporate governance including the composition of board, appointment of new directors, review of strategic human resource decisions, succession planning for the chairman and other key board and executive positions, performance evaluation of the board and its committees and individual directors.

A company may constitute this Committee to develop and recommend the board a set of corporate governance guidelines applicable to the company, implement policies and processes relating to corporate governance principles, to review, periodically, the corporate governance guidelines of the company.

RISK MANAGEMENT COMMITTEE

A company needs to have a proactive approach to convert a risk into an opportunity. A business is exposed to various kind of risk such as strategic risk, data security risk, fiduciary risk, credit risk, liquidity risk, reputational risk, environmental risk, competition risk, fraud risk, technological risk etc. It is important for the company to have a structured framework to satisfy that it has sound policies, procedures and practices are in place to manage the key risks under risk framework of the company. A risk management Committee's role is to assist the Board in establishing risk management policy, overseeing and monitoring its implementation.

REGULATORY, COMPLIANCE & GOVERNMENT AFFAIRS COMMITTEE

The primary objective of the Compliance Committee is to review, oversee, and monitor:

- the Company's compliance with applicable legal and regulatory requirements;
- the Company's policies, programs, and procedures to ensure compliance with relevant laws, the Company's Code of Conduct, and other relevant standards;
- the Company's efforts to implement legal obligations arising from settlement agreements and other similar documents; and
- Perform any other duties as are directed by the Board of Directors of the company.

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