

A welcome directive

Come January 1, promoters will have less room -- and less incentive -- to fill their board with their own

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In about three months, a policy change that has the potential to raise the standards of corporate governance will sweep through India Inc. Come January 1, independent directors – basically, those who don't have any affiliation to a company or its promoters – will have to make up at least 50 per cent of the board of directors of all listed companies.

Why independent directors?

For decades, we have seen promoters blatantly pursue private gains. It's ironical we have many sick companies, but no poor promoters! That's where independent directors come in. They can -- at least, they are expected to -- exert influence to ensure companies comply with legal requirements, don't indulge in malpractices, and act in the interests of non-promoter shareholders. Given their 'big brother' mandate, it is important to not only have independent directors on company boards, but also give them the numbers to influence. Of course, some professionals, with their own areas of expertise, add value to a board -- thereby increasing shareholder value.

But many among the 'old generation' oppose the concept of independent directors. They don't want strangers being privy to their decisions. They say an external director's knowledge about the company is limited to a few meetings and he may, just to prove a point, stall even good policies. Fact remains, most companies have more to conceal than reveal, which explains their opposition. As a stalling tactic, in fact, some people are pitching Sebi against the ministry of company affairs (MCA) on this subject.

Degrees of independence

Meanwhile, there are several other issues. Like, do independent directors truly exist? Sebi defines an independent director as one who doesn't have any material relationship with the company, its promoters, directors and senior management, or its holding company, subsidiaries and associates. But still, promoters can compromise on the spirit of 'independence'. Promoters have been known to appoint only people known to them. They pay them well for their services and get them to toe their line. Remuneration for independent directors is a ticklish question -- it shouldn't be so low as to disinterest competent persons from accepting board positions nor too high to impact their independence.

Most companies will meet the deadline and get people within their control on board. The top companies, being well connected, will easily find such people who are also competent. The bottom companies will hire friends and relatives, whether qualified or not, to meet the requirement. That said, more and more companies are realising that good governance makes good business sense. Many are also conscious about the public reaction and analysis that is inevitable after December 31. Such companies are inclined to pick professionals who will add to the business and also build confidence among investors.

Scarcity or scared?

Some industry associations, ostensibly at the behest of companies they represent, say there is a paucity of qualified professionals. Not true. We have thousands of professionals who are qualified and willing. The problem is finding them. Companies can contact only those persons known to them or through word-of-mouth, thereby limiting their search. Thousands of competent professionals are willing, but how do they let the listed companies know about themselves?

Some months ago, the National Foundation for Corporation Governance (NFCG) asked the apex chambers and professional bodies to prepare a database of independent directors. Not much happened. A website launched last week, www.primedirectors.com, addresses the issue of how to reach out to professionals (disclosure: I am involved with the site). This site is a free-of-charge platform where professionals interested in directorship can enrol themselves in the database, through which listed companies can browse and identify potential candidates.

One issue, though, needs to be addressed. There have been cases of independent directors being implicated despite not being involved with their company's day-to-day running, courts issuing non-bailable warrants against former directors because the promoters-directors ignored a summons. Non-executive directors not involved in a company's day-to-day running shouldn't be held responsible for all its actions. After all, they don't have access to all information. But if they are aware of any negative development and stay silent, they should be held accountable.