Exodus of independent directors looms

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India Inc may be staring at an exodus of independent directors this financial year, amid the changing regulatory landscape.

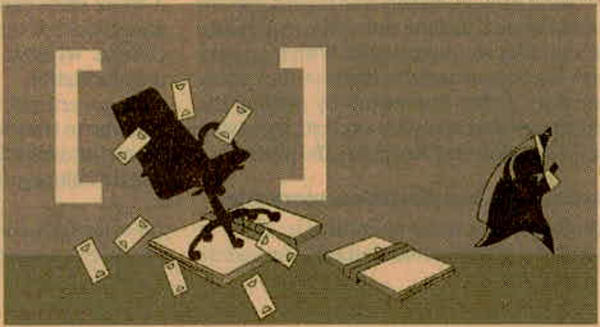
In the past year, more than 1,000 independent directors have quit, spooked by high-profile corporate frauds, accounting discrepancies, and application of global anti-corruption laws. In the past two months alone, about 400 independent directors have quit as against 200 appointed, hinting at a likely widening gap between demand and supply that might play out in the coming months.

About 1,500 independent directors had signed up for five-year terms in 2014-15, which are up for renewal this year. Independent directors can get a second term after approval by a special resolution.

"Many of these independent directors may opt not to extend their tenure, given the greater accountability and increasing liability they might face," said Shriram Subramanian, founder and managing director, InGovern Research Services.

The Companies Act, 2013, effective April 1, 2014, had laid out a separate code for independent directors. The recent change in listing regulations based on the recommendations

ILLUSTRATION: BINAY SINHA



INDIA INC STORY

	Cessations	Appointments		Cessations	Appointments
Jan,'18	46	84	Sep,'18	65	43
Feb,'18	69	91	Oct,'18	50	72
Mar,'18	70	62	Nov,'18	72	80
Apr,'18	50	57	Dec,'18	45	36
May,'18	96	122	Jan,'19	46	59
Jun,'18	60	40	Feb,'19	69	115
Jul,'18	52	87	Mar,'19	243	87
Aug,'18	93	98	Apr,'19	151	122

*from NSE listed companies

Source: PRIME Database

of the Kotak Committee has also bolstered governance requirements. The role of independent directors in fraud detection has come under the regulators' scrutiny as they, along with auditors, are the first line of independent authorities obliged to question wrongdoing early in the day. Independent directors carry both legal and regulatory obligations to raise red flags and record dissent on board matters.

"There is now an increasing appreciation that while the role of an independent director is appealing, it casts significant responsibility on them, which, if not discharged appropriately, exposes them to significant risk," said Sai Venkateshwaran, partner and head-CFO Advisory, KPMG in India.

Directors can be liable to face class action suit under the Companies Act, criminal misappropriation under Section 403 of the Indian Penal Code (IPC), and criminal breach of trust under Section 405 of the IPC. There could also be scenarios where an independent director on the board of a wilful defaulter — for not showing dissent or for failing to act — might get tagged as a defaulter in his personal capacity as a director. This could result in him being declared not fit and proper to hold any significant position in a financial intermediary or carry out any financial regulatory activity.

"Independent directors are more conscious of their responsibilities, duties, and liabilities. In audit committees, one sees more surveillance and vigilance, particularly on related party transactions. While there has been a positive change, however, there is still a long way to go," said Vinod Kothari, managing partner, Vinod Kothari & Company.

In case of an egregious resolution, the regulator or a minority shareholder could take the independent directors to court and take them to task for not opposing the resolution. This is particularly true of related party transactions (RPTs).

"RPTs are a huge item for independent directors; to first track who a related party is and to ensure that the transactions are done at fair market prices for both entities. While the independent directors have the power to ask an external auditor to validate the price, the auditor itself may not be truly independent," said Arvind Sethi, an independent director.

Some directors are now taking efforts to do due diligence on companies before signing up for new directorships. Independent directors are also documenting their consent or dissent as appropriate on various decisions subject to board processes, and taking steps to ensure their personal assets are ring-fenced. Companies, for their part, are taking adequate cover under the directors and officers insurance policies to provide necessary protection to their independent directors.

"Measures such as indemnity bonds executed by the company or the promise to compensate in any manner (including damages) should be contemplated. Independent directors should be provided immunity and protection except in cases of wilful fraud or gross neglect," said Souvik Roy, partner, IC Universal Legal.

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