

Note on Independent Director

❖ INTRODUCTION:

Corporate Governance structure had been re-shuffled post induction of requirement for appointment of Independent Director in the Board of Company as Non-executive independent directors with motive for prevention of the concentration of power in one individual person or over influence in the Company management i.e. to provide “act of balancing of power” in the public interest. In this article, we look at the position, role, functions, duties, liabilities and so on related to an Independent Director of a company.

❖ BACKGROUND:

This idea and concept of Independent Director gained prominence in India in the year 2000, when SEBI mandated that all major publicly listed Companies have a minimum number of independent directors on their boards. This requirement followed the approval of Clause 49 of listing agreement, which deals with corporate governance, by the Kumar Mangalam Birla committee. Later, other committees such as the Narayan Murthy Committee and the Naresh Chandra Committee were established. thereafter introduction of the Companies Act, 2013.

❖ REQUIREMENT OF APPOINTMENT OF INDEPENDENT DIRECTOR:-

As per the provisions of sub section (4) of Section 149 of the Companies Act 2013:-

- i. All listed public limited companies are mandatorily required to have at least one-third (1/3rd) of the total number of directors as an Independent Directors.
- ii. All Unlisted public companies should appoint at least two independent directors in the following situations:
 - a. If the paid up share capital is in excess of Rs.10 crores. Or
 - b. If the turnover is in excess of Rs.100 crores. Or
 - c. If the total of all the outstanding loans, debentures and deposits is in excess of Rs 50 crores.

Further stated that in case a company is required to appoint a higher number of independent directors due to composition of its audit committee, such higher number of independent directors shall be applicable to it:

❖ **EXEMPTION FROM APPOINTMENT OF INDEPENDENT DIRECTOR:-**

The following classes of unlisted public company shall not be required to appoint Independent Director:-

- (a) a joint venture;
- (b) a wholly owned subsidiary; and
- (c) a dormant company as defined under section 455 of the Act.

❖ **QUALIFICATION OF INDEPENDENT DIRECTOR:-**

Independent Director” means an independent director referred to in sub-section (6) of section 149 of the Companies Act, 2013;

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,—

- (a)** who, in the opinion of the Board, is a person of integrity and possesses relevant expertise and experience;
- (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;
- (c)** who has or had no pecuniary relationship, other than remuneration as such director or having transaction not exceeding ten per cent. of his total income or such amount as may be prescribed,] with the company, its holding, subsidiary or associate company, or their promoters, or Directors, during the two immediately preceding financial years or during the current financial year;]
- (d)** none of whose relatives—
 - (i) is holding any security of or interest in the company, its holding, subsidiary or associate company during the two immediately preceding financial years or during the current financial year: Provided that the relative may hold security or interest in the company of face value not exceeding fifty lakh rupees or two per cent. of the paid-up capital of the company, its holding, subsidiary or associate company or such higher sum as may be prescribed;
 - (ii) is indebted to the company, its holding, subsidiary or associate company or their promoters, or Directors, in excess of such amount as may be prescribed during the two immediately preceding financial years or during the current financial year;
 - (iii) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, its holding, subsidiary or associate company or their promoters, or Directors of such holding company, for such amount as may be prescribed during the two immediately preceding financial years or during the current financial year; or
 - (iv) has any other pecuniary transaction or relationship with the company, or its subsidiary, or its holding or associate company amounting to two per cent. or more of its gross turnover or total income singly or in combination with the transactions referred to in sub-clause (i), (ii) or (iii);]
- (e)** 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;

Provided that in case of a relative who is an employee, the restriction under this clause shall not apply for his employment during preceding three financial years.]

(ii) 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 the company or its holding, subsidiary or associate company; or

(B) any legal or a consulting firm that has or had any transaction with the company, its holding, subsidiary or associate company amounting to ten per cent. or more of the gross turnover of such firm;

(iii) holds together with his relatives two per cent. or more of the total voting power of the company; or

(iv) is a Chief Executive or director, by whatever name called, of any nonprofit organisation that receives twenty-five per cent. or more of its receipts from the company, any of its promoters, Directors or its holding, subsidiary or associate company or that holds two per cent. or more of the total voting power of the company; or

(f) who possesses such other qualifications as may be prescribed.(Rule 5 of the Companies (Appointment and Qualification of Directors), 2014

Qualifications of Independent Director

(1) An independent director shall possess appropriate skills, experience and knowledge in one or more fields of finance, law, management, sales, marketing, administration, research, corporate governance, technical operations or other disciplines related to the company's business.

(2) None of the relatives of an independent director, for the purposes of sub-clauses (ii) and (iii) of clause (d) of sub-section (6) of section 149,-

(i) is indebted to the company, its holding, subsidiary or associate company or their promoters, or directors; or

(ii) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, its holding, subsidiary or associate company or their promoters, or directors of such holding company, for an amount of fifty lakhs rupees, at any time during the two immediately preceding financial years or during the current financial year

Further **Rule 6** of the Companies (Appointment and Qualification of Directors),2014

Compliances required by a person eligible and willing to be appointed as an independent director.

✚ **Section 150** of the Companies Act, 2013 provides that “an independent director can be selected from a data bank maintained by any-body, institute or association, as may be notified by the Central Government. The data bank would contain names, addresses and qualifications of persons who are eligible and willing to act as independent directors. The company needs to ensure exercise of due diligence before selecting an independent director from the data bank”

✚ **The Companies (Appointment and Qualification of Directors) Fifth Amendment Rules, 2019 effective from 1st December, 2019** require the existing Independent Directors as well as the

professionals aspiring to become independent directors, **to apply online to IICA for inclusion of their name with the Independent Directors Databank** for a period of one year or five years or for his life-time, and from time to time take steps as specified in sub-rule (2), till he continues to hold the office of an independent director in any company:

✚ ***Upon registration the individuals are required to pass a online proficiency self-assessment test within a period of 2 year from the date of inclusion of his name in the data bank, failing which, his name shall stand removed from the databank of the institute.***

✚ **Exemption from passing online proficiency self-assessment test has been granted to individuals:**

An individual shall **not be required to pass** the online proficiency self-assessment test when **he has served for a total period of not less than three years** as on the date of inclusion of his name in the data bank,-

(A) as a director or key managerial personnel, as on the date of inclusion of his name in the databank, in one or more of the following, namely:-

(a) listed public company; or

(b) unlisted public company having a paid-up share capital of rupees ten crore or more; or

(c) body corporate listed on any recognized stock exchange or in a country which is a member State of the Financial Action Task Force on Money Laundering and the regulator of the securities market in such member State is a member of the International Organization of Securities Commissions; or

(d) bodies corporate incorporated outside India having a paid-up share capital of US\$ 2 million or more; or

(e) statutory corporations set up under an Act of Parliament or any State Legislature carrying on commercial activities; or

(B) in the pay scale of Director or equivalent or above in any Ministry or Department, of the Central Government or any State Government, and having experience in handling,—

C) in the pay scale of Chief General Manager or above in the Securities and Exchange Board or the Reserve Bank of India or the Insurance Regulatory and Development Authority of India or the Pension Fund Regulatory and Development Authority and having experience in handling the matters relating to corporate laws or securities laws or economic laws :

Provided also that the following individuals, who are or have been, for at least ten years :—

(A) an advocate of a court; or

(B) in practice as a chartered accountant; or

(C) in practice as a cost accountant; or

(D) in practice as a company secretary, shall not be required to pass the online proficiency self-assessment test.

❖ **ROLE & DUTIES OF INDEPENDENT DIRECTORS:-**

The guidelines, role, functions and duties of an Independent Director is defined in the **Code of conduct** under **Schedule IV** of the Companies Act, 2013.

Independent Director acts as a guide, coach, and mentor to the company. The role includes improving corporate credibility and governance standards by working as a watchdog and help in managing risk. Independent directors are responsible for ensuring better governance by actively involving in various committees set up by the company.

The independent directors are required because they perform the following important roles:

- (i) To help in bringing an independent judgment to bear on the Board's deliberations especially on issues of strategy, performance, risk management, resources, key appointments and standards of conduct;
- (ii) To bring an objective view in the evaluation of the performance of board and management;
- (iii) To scrutinize the performance of management in meeting agreed goals and objectives and monitor the reporting of performance;
- (iv) To satisfy themselves on the integrity of financial information and that financial controls and the systems of risk management are robust and defensible;
- (v) To safeguard the interests of all stakeholders, particularly the minority shareholders;
- (vi) To balance the conflicting interest of the stakeholders;
- (vii) To determine appropriate levels of remuneration of executive Directors, key managerial personnel and senior management and have a prime role in appointing and where necessary recommend removal of executive Directors, key managerial personnel and senior management;
- (viii) To moderate and arbitrate in the interest of the company as a whole, in situations of conflict between management and shareholder's interest.

The Duties of Independent Directors:-

- (i) undertake appropriate induction and regularly update and refresh their skills, knowledge and familiarity with the company;
- (ii) seek appropriate clarification or amplification of information and, where necessary, take and follow appropriate professional advice and opinion of outside experts at the expense of the company;
- (iii) strive to attend all meetings of the Board of Directors and of the Board committees of which he is a member;
- (iv) participate constructively and actively in the committees of the Board in which they are chairpersons or members;
- (v) strive to attend the general meetings of the company;
- (vi) where they have concerns about the running of the company or a proposed action, ensure that these are addressed by the Board and, to the extent that they are not resolved, insist that their concerns are recorded in the minutes of the Board meeting;

- (vii) keep themselves well informed about the company and the external environment in which it operates;
- (viii) not to unfairly obstruct the functioning of an otherwise proper Board or committee of the Board;
- (ix) pay sufficient attention and ensure that adequate deliberations are held before approving related party transactions and assure themselves that the same are in the interest of the company;
- (x) ascertain and ensure that the company has an adequate and functional vigil mechanism and to ensure that the interests of a person who uses such mechanism are not prejudicially affected on account of such use;
- (xi) report concerns about unethical behaviour, actual or suspected fraud or violation of the company's code of conduct or ethics policy;
- (xii) acting within his authority, assist in protecting the legitimate interests of the company, shareholders and its employees;
- (xiii) not disclose confidential information, including commercial secrets, technologies, advertising and sales promotion plans, unpublished price sensitive information, unless such disclosure is expressly approved by the Board or required by law.

❖ **OTHER PROVISIONS AND COMPLIANCE RELATED TO INDEPENDENT DIRECTORS UNDER COMPANIES ACT, 2013:-**

1. **Declarations by ID:-** Every independent director shall at the first meeting of the Board in which he participates as a director and thereafter at the first meeting of the Board in every financial year or whenever there is any change in the circumstances which may affect his status as an independent director, give a declaration that he meets the criteria of independence as provided in sub-section (6) of Section 149 of the Companies Act, 2013.
2. **Remuneration or Sitting Fees to ID:-** Independent director shall not be entitled to any stock option and may receive remuneration by way of fee provided under sub-section (5) of section 197, reimbursement of expenses for participation in the Board and other meetings and profit related commission as may be approved by the members. Further if a company has no profits or its profits are inadequate, an independent director may receive remuneration, exclusive of any fees payable under sub-section (5) of section 197, in accordance with the provisions of Schedule V.
3. **Appointment or Re-appointment of ID on the Board of Company:-**
 - i. an Independent director shall hold office for a term up to 5 consecutive years on the Board of a company, but shall be eligible for reappointment on passing of a special resolution by the company and disclosure of such appointment in the Board's report.

- ii. No independent director shall hold office for more than two consecutive terms, but such independent director shall be eligible for appointment after the expiration of three years of ceasing to become an independent director.
- iii. Further independent director shall not, during the cooling period of three years, be appointed in or be associated with the company in any other capacity, either directly or indirectly.

4. Independent Directors Roles in Various Committee:-

- i. The Audit Committee shall consist of a minimum of three Directors with independent Directors forming a majority.
- ii. The Board of Directors of every listed public company and such other class or classes of companies, as may be prescribed shall constitute the Nomination and Remuneration Committee consisting of three or more non-executive Directors out of which not less than one-half shall be independent directors.
- iii. The constitution of a Corporate Social Responsibility Committee of the Board shall consist of three or more Directors, out of which at least one [director](#) shall be an independent director.