

Development of Corporate Jurisprudence in India

The Way Forward

SOMASEKHAR SUNDARESAN

January 29, 2017

CONTEXT OF REGULATION

- Governance deficit is a society-wide phenomenon
- Indian political economy entails legislating virtue
- Legislative disincentives are thought as solutions
- Best practices are made statutory requirements
- Emphasis on criminalizing undesirable conduct
- State capacity constraints almost never factored in
- Regulatory race leading to differential criteria
- Every scam leads to clamour for greater powers
- Generic powers to inflict serious injury conferred

BOARD COMPOSITION

- Primary regulation of governance is with board composition
 - *securities regulations run in parallel*
- Board composition for listed companies intensely regulated
 - *one-third to be “independent directors”*
 - *Section 149 defines term with stringent criteria*
 - *5-year term; 2 successive terms; 3-year cool-off*
 - *annual declaration of independent status*
- At least one resident Indian director - new requirement
- Social justice interventions too are mixed up
 - *woman director; small shareholder director*
- At least two-thirds to retire by rotation

COMPANY LAW PROVISIONS

- Not more than twenty directorships allowed
 - *public company directorships not to exceed ten*
- Section 166 has motherhood objectives
 - *promote benefits of members as a whole*
 - *interests of company, employees, shareholders, community and environment protection*
- Mandatory committees for listed companies
 - *overlap with securities regulatory requirements*
- Regulation of related party contracts
 - *shareholder approval if outside ordinary course; or*
 - *if not on arms-length terms*
 - *Audit Committee to approve*

SECURITIES REGULATIONS

- Listing agreement had governance conditions
 - *now elevated to Listing Regulations*
- Composition norms more detailed and granular
 - *at least one-half to be non-executive*
 - *one-third or one half to be independent*
- Special sub-committees are mandatory
 - *Audit Committee - financially literate*
 - minimum 3 members; 2/3rd, and chairman, independent
 - *Nomination and Remuneration Committee*
 - all non-executive; 3 members; all non-exec; 50% independent
 - *Risk Management Committee*
 - may comprise non-directors - chair to be a director

SUBSIDIARIES OF LISTED COS.

- Governance of subsidiaries of listed companies regulated too
 - *at least one independent director from listed company board to sit on material subsidiary board*
 - *minutes of unlisted subsidiaries to be tabled with the board of the listed company*
 - *statement of “significant transactions and arrangements” to be given to listed company board*
 - more than 10% of the revenues, expenses, assets or liabilities
- Listed Co. shareholder approval needed for:-
 - *disposal of assets of above 20% of subsidiary*
 - *disposal of subsidiary shares to de-subsidiarize it*

OTHER SECURITIES REGULATIONS

- Board of Directors have special obligations
 - *to make recommendation on open offer terms*
 - *not take material decisions once offer is made*
 - *to ensure subsidiaries comply*
- Recusal from discussions / preparations
 - *at the target's board if linked to acquirer*
 - *at the acquirer's board if linked to target*
- Listed boards to apply their mind in designating insiders for compliance coverage
- Listed boards to frame specific policies
 - *essentially, no delegation is permitted on issues*

OTHER REGULATORS

- Interplay of shareholder agreements and “control”
- Sectoral regulators add to corporate governance obligations
 - *Insurance regulator has its guidelines on directorships and tenure*
 - *RBI often requires board attention to specific issues of policy*
 - *Ministry of Finance Circulars specify what boards of nationalised banks should discuss*
 - *Nayak Committee Report found that they only discussed those*
- Increased resort to subordinate legislation enables prescription of even more requirements for boards in various sectors
- Company law already provides for endorsement in Directors’ Responsibility Statement
 - *that proper systems were devised*
 - *to comply with all applicable laws*
 - *such systems were adequate and operating effectively*
- A sectoral violation could become a company law violation

CONSTITUTIONAL ISSUES

- Company law is through Act of Parliament
- Listing Regulations under SCRA and SEBI Act
 - *two statutes administered by the same regulatory body*
- So, same facts could lead to triple-tracked action
 - *action under Listing Regulations alone could lead to two parallel enforcement processes being invoked*
- Example of Prevention of Money Laundering Act
 - *SEBI and RBI are only authors of circulars under PMLA*
 - *SEBI invoked Section 11 in its circular*
 - *punishment under SEBI Act on grounds of market “hygiene”*
 - *Securities Appellate Tribunal has upheld the action*
 - *penalty too tiny for actionee to challenge question of law*
- Future litigation will occur around constitutional challenge to scale, scope and multiplicity of powers for the same actions

FUTURE OF JURISPRUDENCE

- Tribunalisation of corporate jurisprudence
- Appeals from NCLAT lie in the Supreme Court
- Writs are the only exposure to High Courts
- Jurisdiction ranges from regulatory to suits
 - Petitions for oppression and mismanagement
 - Schemes of Arrangement
 - Winding up, bankruptcy and insolvency
 - Class action suits

Q&A

som@somasekhar.in