

## **SEBI's Announcement on Independent Directors**

### **Why in news?**

SEBI (Securities and Exchange Board of India) has backtracked on its earlier proposal of “dual approval” system in appointing independent directors.

### **Who are independent directors?**

- Positions of independent directors were created in corporate boards to address corporate frauds and mis-governance issues.
- An Independent director is a non-executive director.
- S/he does not have any kind of relationship, material or financial, with the company.
- Independent directors are to ensure the independence of decisions taken in matters related with the board.
- A larger say for independent directors was believed to have an effective deterrent to fraud, mismanagement, and mis-governance.

### **How are independent directors appointed?**

- An independent nomination and remuneration committee of the board screens candidates for independent directorships.
- But independent directors are appointed just like other directors through shareholder voting by a simple majority.
- In case of family-owned companies, it is common to appoint “friendly” independent directors.
- **Concerns** - The process for appointment and removal of independent directors is by far the most important determinant of allegiance.
- Shareholder voting by a simple majority confers significant power in the hands of significant shareholders to handpick the independents.
- So, independent directors owe their allegiance merely to the promoters and not to the shareholder body as a whole.
- As for public sector undertakings, a study reveals a demonstrable affiliation between independent directors and the ruling political power.

### **What was SEBI's dual approval system in this regard?**

- The SEBI, in March 2021, in its consultation paper, proposed a “dual approval” system.

- Under this, the appointment of an independent director required the satisfaction of two conditions:
  1. the approval by a majority of all shareholders
  2. the approval of a “majority of the minority”, namely the approval of shareholders other than the promoters
- In case of a failure to satisfy the two-step test, the company would be free to propose the same candidate after a 90-day cooling off period.
- It should go for approval by a special resolution (75% majority) of all shareholders voting.
- SEBI recommended the same “dual approval” system for the removal of independent directors as well.
- The dual approval system draws inspiration from Israel and the premium-listed segment of the United Kingdom.
- They confer greater power to minority shareholders in installing or dethroning independent directors.

### **What is the recent announcement?**

- SEBI announced that the appointment and removal of independent directors would be by way of a special resolution rather than a simple majority.
- It made no mention of the dual voting system.
- By this, SEBI has clearly backtracked from its earlier proposal.
- It deprived the minority shareholders of the level of say it had extended earlier.
- In all, the appointment and removal system continues to undermine the independence and efficacy of corporate boards.

**Source: The Indian Express**

