

Kotak Committee Report : Proposed reforms in Corporate Governance norms

Introduction:

In a extremely proactive step to further improving the corporate governance framework in India, the Securities and Exchange Board of India ('SEBI') formed a committee on Corporate Governance ('Committee) in June 2017 under the chairmanship of none other than Mr. Uday Kotak with a view to provide recommendations for enhancing the standards of Corporate Governance of listed companies in India. The Committee consisted of officials from the government, industry, professional bodies, stock exchanges, academicians, lawyers, proxy advisors, etc.

The terms of reference of the committee were to make recommendations to SEBI on the following issues which inter-alia includes:

- Ensuring independence in spirit of Independent Directors and their active participation in functioning of the Company;
- Improving safeguards and disclosure pertaining to Related Party Transactions;
- Issues in accounting and auditing practices by listed companies;
- Addressing issues faced by investors on voting and participation in general meetings.

The Committee's approach to the recommendations has been driven by the primary objective of enhancing corporate governance for listed entities. In this regard, the Committee believes that there are certain recommendations which may require implementation by authorities/ regulators in addition to SEBI. Therefore, the Committee has suggested that SEBI take up such recommendations with the relevant authorities/ regulators.

The Committee had received the observations/comments/objections/suggestions on the recommendations from Ministry of Corporate Affairs (MCA) and Ministry of Finance (MoF) on October 3, 2017 i.e. before submission of recommendations to SEBI. A significant number of recommendations by the Committee conflict with the provisions of the Companies Act, 2013 and face dissent from MCA (say 12 dissents out of 24 recommendations on the Board of Directors alone) and other regulatory bodies such as the Institute of Chartered Accountants of India (ICAI).

The Key recommendations of the Committee are summarized as follows:

Particulars	Committee's Key recommendations	Proposed Effective date
Composition and Role of the Board of Directors		
Minimum Number of Directors	Minimum 6 Directors on the Board with at least 1 Woman Director. Out of which half of the board shall comprise of Independent Directors by;	01.10.2018

	<p>a) top 500 listed entities, determined on the basis of market capitalization, as at the end of the immediately preceding financial year;</p> <p>b) all other listed entities.</p>	<p>01.01.2019</p> <p>01.01.2020</p>
Number of Board/Committee meetings and quorum for Board meetings	<p>At least 5 (Five) Board and Audit Committee meetings and at least 1 (One) meeting in respect of Nomination and Remuneration Committee, Stakeholders Relationship Committee and Risk Management Committee shall be held during the year.</p> <p>The quorum for the Board meeting shall be one-third of its total strength or three directors, whichever is higher, including at least one Independent Director.</p> <p>The quorum for a meeting of NRC and SRC shall be either 2 members or 1/3rd of the members of the committee, whichever is greater, with at least 1 ID.</p>	<p>01.04.2018</p> <p>01.10.2018</p> <p>01.04.2018</p>
Attendance of Directors	Attendance of each Director is must in at least half of the Board meetings held during a period of 2 consecutive financial years on a rolling basis. If not present, his/her continuance on the board should be ratified by shareholders at next Annual General Meeting (“AGM”).	01.04.2018
Continuance of Non-Executive Directors beyond certain age	As is the case of Managing/Whole-time Directors continuance, the continuance of Non-Executive Directors who are attaining age of 75 years, requires approval of shareholders by way of passing of Special resolution at the general meeting.	01.10.2019
Separate post for Chairman and Managing Director	<p>Non-executive director should be chairperson in case of listed entities which have public shareholding of 40% or more w.e.f. 01.04.2020.</p> <p>After 2020, all listed entities should have non-executive directors as chairperson, if deemed fit by SEBI.</p>	<p>01.04.2020 /</p> <p>01.04.2022</p>
Independent Directors (IDs)		
Minimum compensation to Independent Directors	Minimum compensation to be paid to Independent Directors on the basis of market capitalisation for top 500 listed entities.	01.04.2018
Prohibition of Alternate Director for IDs	The appointment of an alternate director for Independent Directors should not be permitted.	01.04.2018

Lead ID	All listed entities which have a non-independent chairperson shall designate an Independent director as the lead Independent Director.	01.10.2018
Board Committees		
Composition	The composition of Board committee shall be as follows: a. NRC – 2/3 rd of members shall be IDs; b. SRC – At least 3 Directors with at least 1 being ID.	01.04.2019
Limit of membership / chairmanship	Inclusion of chairmanship and membership of Nomination and Remuneration Committee for the purpose of determining the limit of total number of chairmanship and membership.	01.04.2018
Enhanced monitoring of group entities		
Material Subsidiary definition	Amendment of the definition of “material subsidiary” by amendment of percentage of the income or net worth of the subsidiary with consolidated income or net worth, of the listed entity and its subsidiaries from existing of 20% to 10%. However, for the purpose of regulation 24 (Corporate governance requirements with respect to subsidiary of listed entity), the percentage remains 20% of income or net worth of the subsidiary with consolidated income or net worth, of the listed entity and its subsidiaries for the purpose of “material subsidiary”.	01.04.2018
Secretarial Audit	Compulsory Secretarial Audit for all material unlisted Indian subsidiaries.	01.04.2018
Promoters/Controlling shareholders and Related Party Transactions		
Disclosure of Related party transactions	Half yearly disclosure of Related party transaction on consolidated basis, within 30 days of publication of the half yearly financial results on the website of company and submission to stock exchange. Also, it recommends that, all promoter/promoter group entities that hold 20% or above in a listed entity to be considered as “related parties” for the purpose of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (“ LODR ”).	01.04.2018

Approval of Related party transactions	Removal of blanket ban on related parties to vote on resolutions and suggest for allowing the related parties to cast only negative vote, if they desire to dissent on such resolution.	With immediate effect upon acceptance of proposal
Royalty and Brand payments to Related parties	The prior approval from shareholders is required on “majority of minority” basis if payment for brands usage/royalty amount exceeds 5% of consolidated turnover of listed entity.	01.04.2018
Disclosures and Transparency		
Submission of Annual Report	The copy of annual report shall be submitted to the Stock Exchange not later than the day of commencement of dispatch to its shareholders and in the event of shareholders approves any amendments to any portion of Annual report, then the revised copy to be submitted not later than 48 hours after the AGM.	01.04.2018
Manner of sending Annual report to shareholders	Compulsory dispatch of Annual report in soft copy at email address(es) of shareholders registered either with the listed entity or with any depository, unless any shareholder request for specific mode of dispatch.	01.04.2018
Searchable formats of Disclosures	All disclosures made by the listed entity to the stock exchanges shall be in XBRL format and upload the same in any searchable format on its website.	01.04.2018
Harmonization of Disclosures	The stock exchanges shall collectively harmonize the formats of the disclosures made by the listed entities and a common filing platform may be devised on which a listed entity may submit all filings, which could then be disseminated to all exchanges simultaneously. Further, the disclosures filed with the exchanges may, as far as possible, be harmonized with the filings made to MCA.	01.04.2018
Disclosure of key changes in Financial indicators	All listed entities may be required to disclose on the section of Management Discussion and Analysis in the Annual report, certain key financial ratios, wherever there is a change of 25% or more in a particular financial year along with details of any change in return on Net worth as compared to the immediately previous financial year.	01.04.2018
Disclosure pertaining to Disqualification of Directors	A disclosure in Corporate Governance report is required to be made regarding directors of the listed entity not having been debarred or disqualified from being appointed or continuing as directors of companies by the SEBI/MCA or any such statutory authority based on certificate availed from a company secretary in practice.	01.04.2018
Disclosure of Subsidiary accounts	The separate audited financial statements of each subsidiary of the listed entity in respect of relevant financial year, to be uploaded at least 21 days prior to the date of AGM.	01.04.2018
Prior intimation for Bonus issue	Proposal to remove the proviso under regulation 29 which states that prior intimation is not required in case of declaration of bonus by listed entity if not on the agenda of the meeting of board of directors.	With immediate effect upon

		acceptance of proposal
Accounting and Audit related issues		
Independent External opinion by Auditors	In case where the auditor does not concur with the opinion of an expert appointed by listed entity, the auditors should have a right to obtain independent external opinions as deemed fit, at the cost of the listed entity.	01.04.2018
Disclosure on services render by Auditor	The total fees paid to auditor and its network entity/network firms of which auditor is a part for availing audit/non-audit services by listed entity shall be disclosed in Annual report on consolidated basis (i.e. fees paid by the listed entity and its subsidiaries).	01.04.2018
Disclosure of credentials and audit fee of auditors	The notice being sent to shareholders should contain certain minimum disclosure in relation to the credentials and terms of appointment of the auditors who are proposed to be appointed/re-appointed although this item is in nature of ordinary business in the annual general meeting.	01.04.2018
Investor participation in meetings of listed entities		
Timeline for holding AGM	It is proposed that the timeline for holding AGM shall be: <ul style="list-style-type: none"> Initially within 5 months from end of financial year i.e. by 31st August 2018, by top 100 listed entities by market capitalization; over a time, the target may be reduced to 4 months from end of financial year i.e. 31st July every year. The same may be extended to other entities in a phased manner based on the experience gained.	01.04.2018
E-voting and webcast of proceeding of the general meetings	<ol style="list-style-type: none"> Live webcast of all general meetings may be introduced for top 100 listed entities on trial basis; E-voting should be kept open till midnight (11.59 p.m.) on the day of general meeting. 	01.04.2018

Conclusion:

Mr. Uday Kotak led Committee has suggested major changes in the current corporate governance scenario in the country. Many of its recommendations, if accepted, are going to change the way the corporate boards function, that is, a paradigm shift from following the 'letter of law' to following the 'spirit of law'. As we can see, the Committee has focussed on enhancing the board processes in interest of stakeholders. It has opened many avenues for active participation of shareholders and transparency in dissemination of information. The independent directors have been put on a higher pedestal by entrusting them with responsibilities in the general affairs of the company. The report also aims to bring a considerable number of entities (that are related to the listed entities), under the purview of SEBI for better monitoring.

The transition that is recommended is quite significant although it is expected to positively change the face of corporate governance practices in India. Understandably, the recommendations of the Committee are well-spanned over a period of few years, to make it easy for the entities to sail through the transformation.

Having taken influence and inspiration from the codes in international jurisdictions, the recommendations of this Committee will have a significant impact on the business practices. Overall, it will metamorphize and strengthen the corporate governance norms, bringing India on the global map of best practices. The proactive step taken to provide Proposed Effective Dates is also a welcome step giving prospective clarity and time to corporates for rearranging their affairs.



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