New Norms for Independent Directors

Why in News

The **Securities and Exchange Board of India (Sebi)** has approved stricter norms related to appointment of **independent directors** and decided to introduce **a framework for accredited investors** along with other measures.

> Sebi is a statutory body established in accordance with the provisions of the **Securities and Exchange Board of India Act, 1992.** The basic functions of the Sebi is to protect the interests of investors in securities and to **promote and regulate the securities market.**

Key Points

Independent Directors:

- Independent directors **can be appointed only through a special resolution** passed by shareholders. A special resolution **requires 75% of votes in favour** to be passed.
- The regulator has also elaborated and strengthened the **disclosure requirements** for **the skills required** to be an independent director.
- The **nomination and remuneration committee** of the board of directors, which decides on appointments and compensation, and the **audit committee** should have **two-thirds independent directors compared to a simple majority now.**
    - All **related party transactions** (between a company and its related entities) **shall be approved by only independent directors** on the audit committee.
- Also, a listed company will be required to **disclose the resignation letter of an independent director.**
    - Also, there will be **a one-year cooling period for an independent director transitioning to a whole-time director** in the same company/holding/subsidiary/associate company or any company belonging to the **promoter group**.

Independent Director

- An Independent Director (also sometimes known as an outside director) is a director on a board of directors **representing minority shareholders** and who does not have a pecuniary relationship with the company or related persons, except for sitting fees.
- Their role is to take a stand unambiguously and independently to have a check and balance on the whims of majority shareholders that may expose the company to unwarranted risks.
- The **Companies Act, 2013** has mandated all **listed public companies to have at least one-third** of the total Directors to be independent.
- Their role requires them to be clinical while businesses expect them to be practical, that's the tight rope they walk on.

- **Accredited Investors:**
  - Sebi has approved this **new category of wealthy, well-informed investors** who will be allowed to **invest in riskier products,** not usually allowed to individuals.
  - These entities (accredited investors) could be individuals, family trusts, proprietorships, etc.
  - They will be given the **flexibility to invest** the less than minimum amount mandated in Sebi rules and also to some extent get relaxation from regulatory requirements.
  - They will enhance the attractiveness of **alternative investment funds (AIFs).**

    AIF means any fund established in India which is a **privately pooled investment vehicle** which collects funds from sophisticated investors, whether **Indian or foreign, for investing** it in accordance with a defined investment policy for the benefit of its investors.
- **Other Important Changes Undertaken:**
  - To provide easy access to investors to participate in **public and rights issues** by using various payment avenues, Sebi has also decided to permit banks, other than scheduled banks, to act as a banker to such issues.

    Unlike initial and follow-up public offering, the rights issue is not open for the general public but only to existing shareholders of the company.
  - Sebi also **increased the maximum reward amount for an informant** who **blows the whistle on insider trading** to Rs 10 crore from Rs 1 crore now.

    Insider trading involves trading in a public company's stock by someone who has non-public, material information about that stock for any reason.
  - The regulator has also approved amendments to its **mutual fund regulations** which requires **asset management companies (AMCs)** to use more funds in riskier schemes (New funds).

    Currently, AMCs have to invest only 1% of the amount raised in a new fund offer, or Rs 50 lakh, whichever is lower.
  - The new norms will be effective **from 1st January, 2022.**

- **Significance:**
  - The changes seek to strengthen the **corporate governance** practices as well as **attract more investors.**
  - It will help **maintain the interest of minority shareholders** in the corporate boardroom where their representation is minimal.
  - This should hopefully result in **truly 'independent' independent directors** and not those with merely a semblance of independence.

Source: IE