

PLATFORM | Madhav Mehra

Keep 'em separated

Independent directors are the cornerstone of good corporate governance. Selecting them wisely is our only hope to instill some discipline in the murky world of corporate finance

WE ARE yet again breeding a culture of greed. One third of a listed company's directors are required to be independent. The erstwhile Company's (Amendment) Bill 2003 had stated that a majority of the minimum seven directors of public companies having share capital in excess of Rs 5 crore should be independent. Clause 49 of the listing agreements defines independent directors as follows: "For the purpose of this clause, the expression 'independent directors' means directors who, apart from receiving director's remuneration, do not have any other material pecuniary relationship or transactions with the company, its promoters, its management or its subsidiaries, which in judgment of the board may affect independence of judgment of the directors."

The key difference between a non-executive director and a non-executive independent director is that the latter is forbidden to have any pecuniary relationship with the company apart from receiving a sitting fee — which at the time of writing that clause was Rs 5,000 and has since been raised to Rs 20,000. Can we truly justify a fee of \$ 450 for a few hours' work in a country where the average wage is less than \$ 3 a day? Do we have consent from shareholders for raising it four times? Perhaps not, because turkeys do not vote for Christmas.

Independent directors are raking in Rs 8-12 lakh a year per company in commission alone. Add to this the sitting fees and the total can be Rs 12-16 lakh. At present, you can be a director on the board of 15 listed companies. So you could be richer by almost Rs 2 crore a year. What is then the difference between a non-executive and an independent director?

Independent directors are the cornerstones of good corporate governance. Theirs is the duty to provide an unbiased, independent, varied and experienced perspective to the board. Corporate scandals of Enron and Worldcom have revealed how this independence has been compromised by a cosy relationship between the CEO even with the so-called independent directors.

The chairman of the audit committee of Enron was no less a person than the Dean of Stanford Business School. Yet, he could not spot the murky goings-on in the company. The same has been true of auditors. Why did auditors of the status of Arthur Andersen allow the deception to continue? In both cases, the independence

was compromised by expectation of excessive rewards. Should we not draw lessons? When a director has developed a stake in a company to the tune of Rs 10-15 lakh a year, would he be able to risk it all by going against the current? This is a hard bat to knock.

We mustn't forget that we're talking of corporate India where a vast majority of listed companies have destroyed shareholders' value. A survey by the Society for Capital Market Research and Development indicated that of the 6,330 BSE listed companies, only 21.5 per cent had paid dividends in 2002-03. Of the 9,644 listed companies, only 16 per cent are dividend paying; 83 per cent of the listed companies in B2 Group, T Group and Z Group have destroyed shareholders value.

A solution to eliminate the cosy relationship between independent directors and their companies can be found by creating an independent body under SEBI. It will be charged with the role of screening and recruiting independent directors and placing them with listed companies. All fees and allowances to the independent directors are paid by the independent organisation under SEBI. The organisation should be funded through a special levy charged by SEBI from each listed company based on the turnover of the company.



CORRECT THE TILT:
Outside the Enron office

In the selection of independent directors, we mustn't look simply for high profile names. The issue is to have someone with an independent state of mind. In an economy fired by innovation, our biggest threat is obsolescence. Periodic training of directors is a must. Unfortunately, there are few courses designed primarily for directors. Warren Buffet recently lamented about the failure of independent directors to protect the interest of shareholders. He blamed the cosy 'boardroom culture' with 'well-mannered people' finding it almost impossible to suggest replacing the chief executive. He said that questioning their remuneration would be like "belching at the dinner table". Independent directors are our only hope to instill some discipline in the murky world of corporate finance. We have to make sure that greed plays no part in their appointment — even if it means belching at the dinner table.

The writer is President, World Council for Corporate Governance