



## Importance of Independent directors in corporate governance and change in their position after Enron Fiasco.

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### Abstract

We learn from various documents and literature that the board of directors should have a pivot role is appointment and removal of key personnel including CEO and decide compensation for all senior management ,design and approve corporate strategy aligning with corporate objectives whereas independent director should be focused on controls for better risk management and to guard the interest of minority shareholders and stake holders ,they need to act tough at the event of any compromise of any measure which dilutes the focus on in the interest of minority shareholders and stakeholder.

Major corporate disasters could not be averted though there was presence of independent directors like in Satyam Enron and WorldCom. The role of Independent directors is very challenging as they need to safeguard the interest of small shareholders having no control on day to day management of the corporate and other stake holder it becomes arduous for them as the Board is more focused on immediate gains and sacrifice of ethical values and requirements which are critical for long term existence of corporates .The role of Independent becoming difficult everyday as expectations are very high with them but there but on many occasions they fail to exercise controls and checks the performance, strategy orientations leading to wide gap between expectations and there performance as stake holders have great expectations what they can do for better corporate governance.

The paper attempts to look into the ways to make independent director effective in most challenging and uncomfortable and dubious circumstances

### Introduction

Normally the presence of Independent Directors in the boardroom gives a feel of confidence in general and inferred as better equipped to address issues of Corporate Governance ,that is the reason globally and in India it is well accepted fact that the presence of Independent Directors would make sure better corporate governance environment. The interest of non-controlling shareholder are better protected by the independent Directors which is always expected with their presence in the board. They are expected to be watchful before the launch of the products in the market .they need to find mechanism to control the shortcomings and manage instead of being over reactive. India gets New Companies act 2013 with enormous power vested under clause 49 of the listing requirements with stock exchanges ,The corporate experience infers that the independent directors were more like puppets in the hands of board of directors.

As per Section 2(47) of the Companies Act, 2013, an „Independent Director' means a Director as referred to in sub-section (5) of section 149. The new Act along with the definition of ID's also provides the criteria for appointing, qualifications, tenure, remuneration and liability of ID's. As per sub-section 6 of Section 149 of the Act, ID means a director other than a managing director or whole time director or a nominee director, a) Who, in the opinion of the Board, is a person of integrity and possesses relevant expertise and experience; b) - 1. Who is or was not a promoter of the company, 2. Who is not related to promoters or directors in the company c) Who has or had no pecuniary relationship with the company d) None of whose relative has or had pecuniary relationship or transaction with the company. e) Who, neither himself nor any of his relative : i. Holds or has held the position of a key managerial personnel ii. Is or has been an employee or proprietor or a partner, in any of the three financial years preceding. iii. Holds together with his relative two per cent or more of the total voting power of the company; or iv. Is a Chief Executive or director, of any nonprofit organization, or who possesses such other qualifications as may b Concept of Independent Director Independence is a quality that can be possessed by individuals and is an essential component of professionalism and professional behavior. It refers to the avoidance of being unduly influenced by a vested interest and to being free from any constraints that would prevent a correct course of action being taken. It is an ability to „stand apart“ from inappropriate influences and to be free of managerial capture, to be able to make the correct and uncontaminated decision on a given issue. Responsibilities and Duties An Independent Director is a person having many years of experience and acts as a guide for the company. The role they play in a company broadly includes improving corporate credibility and governance standards, function as watchdog, play a vital role in risk management. Independent Director plays an active role in various committees to be set up by a company to ensure good governance. Listed companies are required to set up audit committees of minimum three directors, on which, two-thirds should be Independent Director. 1. He should furnish information in the prescribed form to the company about disclosure of General Notice of directorship, membership of body corporate and other entities. 2. He should also inform the company about any change in the details submitted subsequently. 3. He should provide a list of his relatives as defined in the Companies Act and their directorship and interest in other concerns. 4. The Director shall have fiduciary duty to act in good faith and in the interest of the company. 5. It is the duty of the independent director to acquire proper understanding of the business of the company. 6. He should act only within the powers laid down by the Memorandum of Association and Articles of Association and by applicable law and regulations. 7. He should not be a Director of more than fifteen companies. Such an independent director could be working as member of Audit Committee prescribed under Section 292A of the Companies Act. In such situation he has to look into the obligations of Audit Committee and perform the duty as prescribed.

#### Key role of an independent director in a company

- ☑ Board structure and objectivity of the Board
- ☑ Protection of minorities
- ☑ To build up shareholder's confidence in the company
- ☑ To improve relations with investors
- ☑ To make coordinated strategic decisions
- ☑ To resolve conflicts
- ☑ To enhance management transparency
- ☑ To increase company's value
- ☑ Role of other stakeholders in management
- ☑ System of reporting and accountability
- ☑ Audit and internal control
- ☑ Effective supervision and enforcement by regulators

☑ To encourage Sustainable Development of  
the Company and its stakeholders.

Many scams were unearthed during the decade of 2000 to 2010 like Satyam, Enron and WorldCom which led to massive breakdown of financial systems globally led to bail out even in free market economies further massive exploitation of poor & natural resources, massive breach of trusts was witnessed in the global corporate scene in this decade. The large organizations became subject matter of attacks for its power and ill influence was looked like individual greed. The reason for introducing independent directors to enable corporates follow good governance policies and preserve the rights of minority shareholders by being watchful and oversight to prevent any occurrence of exploitation of minority shareholders. The practice of appointing friends and cousins and popular names made a mockery of statutory requirements many of them even did not have requisite qualifications were appointed as independent directors. The professionally managed organizations are run by professionals who also develop strategy the board find it difficult to suggest changes or to find lacuna in the proposed strategy by the CEO due to inexperience in the similar field or technology. CEO normally calls the shots and that remains the culture of the organization and independent directors do not get opportunity to suggest changes CEO prefers a strong advisory board rather than a strong monitoring board, who may be sometimes seen as a constraint for smooth functioning of the business, though the independent director could be stalwart of other area, his intervention may not improve corporate governance. It is a proven fact that the Board as an institution has not been successful and failed miserably in monitoring the protection of minority shareholders' interest.

#### **Conclusion;**

Universally the scenario is not different with respect to appointment of independent directors, the person shall have to act without any fear or favor he needs to be very strong mentally and ethically. He must question anything which he envisages in his professional capacity is against the interest of stakeholders and the same should be recorded. The problem is deep rooted and shall have no easy solution early. But any small move forward shall lead to cover a long journey. Now since it is mandatory to appoint independent directors it is most encouraging step in the right direction of improvement of corporate governance as the 2013 Act has empowered the independent Director fair management operations of the company together with greater accountability as they would have definite say in the management of the company which should make the issue of governance better and it is not necessary that any person who is competent is appointed would bring all the change it all depends on concerted effort of all directors executive, non-executive should work as a team and entire board should make best efforts to work towards creating an ethical environment with keeping in mind of minority shareholders and stakeholders with empathy and broad vision to ensure there is no dent on the corporate image anytime.

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