



ICGN

International Corporate Governance Network

Mr. Sunil Kadam
General Manager
Corporation Finance Department - Division of Issues and Listing
Securities & Exchange Board of India
SEBI Bhavan

By email: anandr@sebi.gov.in & cfddil@sebi.gov.in

31 January 2013

Dear Mr. Kadam,

Re: Consultative Paper on review of Corporate Governance Norms in India

We welcome the opportunity to comment on the changes which the Securities and Exchange Board of India is proposing to corporate governance standards in India. We particularly welcome the focus in the proposals on the obligations of institutional investors and would support the introduction of an Indian stewardship code.

About the ICGN

Below, we outline our responses to the proposals but we would welcome further discussion to elaborate on the points we have made. We attach as appendices some of the ICGN's best practice guidelines to which we refer in this response.

We are particularly supportive of the proposal to introduce a Stewardship Code in India. We have seen such codes lead to significant advances in the effectiveness of dialogue between investors and companies in those markets which have already introduced them. We sincerely hope that India will seize the opportunity to unlock similar improvements. The concept of actively monitoring investee companies through engagement is not widely practised in India; therefore a useful starting point would be for investors to establish guidelines regarding when they will actively intervene at a company to protect and enhance shareholder value.

Our Comments

Strengthening the voice of minority shareholders (relating to proposals 11.1)

Particularly in India, where significant numbers of companies remain dominated by individual founders or their families, it is critical to give minority shareholders confidence that their interests will be protected and that the board focuses on the delivery of value for all shareholders. It is thus of critical importance that the nomination process for the appointment of independent directors for minority shareholder seats and board level directors is conducted in a manner that is credible, transparent and genuinely in line with the interests of minorities. The issue of the protection of minority shareholders features highly in the ICGN's Global Corporate Governance Principles, and we welcome attention being given by SEBI to ways to ensure that minority shareholders' interests genuinely are, and also that investors feel that they are, properly represented at board level.

**Benefits of Board Diversity and Professionalism for board effectiveness
(relating to proposals 11.1, 11.2, 11. 5, 11.6, 11.7, 11.8, 11.10, 11.3, 11.6, 11.15)**

Board Diversity

The ICGN has an ongoing project on the issue of board diversity and will shortly produce a paper in this regard. However, it is already clear that the ICGN's membership is firmly of the view that diversity adds to board effectiveness and thus will help preserve and enhance value. As our Global Corporate Governance Principles set out, effective boards foster challenge and debate, and a diversity of perspectives being brought to bear will make that process of challenge and debate more effective. Diversity in this sense encompasses age, gender, ethnicity, religion and more. One vital aspect of diversity includes international experience and therefore board candidates should not be restricted to Indian nationals.

Usually it will be the role of the chair to ensure that the necessary challenge and debate occurs while also maintaining the spirit of collective endeavour; where the chair is executive or otherwise represents the dominant shareholder this will be more difficult to achieve and the best boards will seek to explain how they deliver this effectively notwithstanding such challenges. We discuss the issue of the dual role of chair/CEO below but these questions extend beyond such circumstances.

Independent judgement of non-executives

We would support excluding nominee directors from the category of independent directors. If a director is appointed under an agreement by an institution or body or by a lender this may create a conflict of interest with the individual feeling accountable only to the organisation they represent rather than acting in the interests of all shareholders.

More widely the nomination committee should consider whether the non-executives are independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, their judgement. Board effectiveness reviews are a valuable regular process formally to consider such questions.

To generate confidence that independent judgement is being applied, a board should include a strong presence of independent non-executive directors with appropriate competencies including key industry sector knowledge and experience. There should be at least a majority of independent directors on the board. The company should state its reasons through the annual report if it determines that a director is independent in spite of the existence of relationships or circumstances which may appear relevant to its determination or a deviation from local best practice. Our Global Principles set out circumstances in which a director's independence may be called into question.

Training for non-executive directors

We commend the encouragement for non-executives to receive ongoing training and the requirement to disclose how this is done. We firmly agree that ongoing training – going beyond the required initial induction process – is a necessary part of the professionalisation of the role of non-executive directors. We believe that this is the overall aim of the SEBI reforms in this area, and we strongly welcome it. We believe other markets could profitably learn from these recommendations.

Tenure and time commitment of directors

As our Global Principles indicate, we would agree that a non-executive serving on a board for greater than 10 years is likely to be regarded as non-independent. If the nomination committee chooses to extend their re-election we

believe that they should be subject to re-election on annual basis, with an explanation given as to their ongoing value to the company.

In order for directors to discharge their fiduciary duties properly and professionally a board should meet at least 7 times within a year and otherwise allocate sufficient time to the company. We would therefore suggest in line with the guidelines issued by the MCA that the maximum number of public companies on which an individual may serve as a director is restricted to around 8; a director will struggle to be effective in more roles than this if the boards are genuinely actively governing and overseeing their companies. We note that other markets around the world have introduced lower limits for multiple directorships and it is likely that investors will actively ask questions about the ability of directors with a number of roles genuinely and professionally to fulfil their fiduciary duties and successfully guide multiple companies to positive business performance.

Age diversity and succession planning

We recognise in the Indian culture the value that mature directors can bring to the cohesion of Indian boards. However age should be considered as part of boardroom diversity with the purpose of having the most capable, dynamic, engaged and committed board members to lead the company to long-term success. Thus there needs to be a mix of ages on boards, just as there needs to be a mix of other attributes; investors are likely to regard the age of any individual director in the context of board structure overall. It is also important to ensure that succession planning for such individuals is actively considered.

Board Leadership (relating to proposals 11.11, 11.12, 11.14, 11.24)

We are generally supportive of splitting the positions of chair and CEO as our global experience tends to indicate that this separation allows the CEO and chair to focus on different, equally vital aspects of the company's performance and offers the best protection for minority shareholders. In response to the SEBI proposals we would suggest that only when the chair is 'independent' is it appropriate for at least one-third of the board to be comprised of independent directors, and that in cases where the chair is an executive director or non-independent non-executive that at least half of the board should comprise of independent directors.

In addition we are supportive of the identification of a lead independent director or deputy chair becoming mandatory across Indian listed companies. In circumstances where the chair is also the CEO, former CEO or otherwise non-independent, the role of the lead independent director is of particular importance in providing independent leadership to the board. In addition, a lead independent director provides an alternative channel to shareholders were their concerns may have failed to be resolved through the chair or CEO. As such it is important that the independent deputy chair or lead independent director makes themselves available to major shareholders to develop a balanced understanding of their views and any issues of concern.

We are supportive of independent directors meeting not only as part of the full board but also separately (apart from management and non-independent directors) at least once a year. The lead independent director should chair this meeting as well as taking a more general role in agreeing the agenda for board meetings, and should have powers to call board meetings and otherwise act as a spokesperson for the independent element of the board.

Board Committees (relating to proposal 11.21)

We would recommend that it should be mandatory that nomination and remuneration committees are separated into the nomination committee and remuneration committee, composed solely of independent non-executive directors. Both have distinct and differing responsibilities which should be given an adequate time for discussion. The remuneration committee plays an important role in ensuring an objective approach to managing executive pay is in place while the nomination committee should lead the process for board appointments and make recommendations to the board on membership, and on whether current directors should be retained.

Remuneration of independent directors & executives (relating to proposals 11.9, 11.22)

We agree that independent directors should not be entitled to any incentive remuneration, because this risks aligning their interests more with the executives than with shareholders.

A remuneration committee should protect and promote the interests of all shareholders when setting executive remuneration. As such disclosures should be made in the annual report on how the executive pay structure and quantum aligns with corporate culture and strategy and serves the interests of long-term value creation.

Risk Management and Audit (relating to proposals 11.17, 11.18, 11.19, 11.20)

It is our firm view that the board is responsible for determining the nature, management and extent of the significant risks it is willing to take in achieving its strategic objectives. The board should be tasked with determining the company's risk-bearing capacity and the tolerance limits for key risks, to avoid the company exceeding an appropriate risk appetite. These should be disclosed appropriately to shareholders as part of the annual reporting process. At certain companies and across certain sectors – particularly those in the financial sectors – it may be advisable to establish a separate risk committee from the audit committee and seek independent advice. The internal auditor should report directly to the audit committee chair.

We are fully supportive of the whistle-blowing safeguards proposed by the MCA guidelines and in particular the adequate protection for employees from being victimised. It is important for such individuals to have access to the chair of the audit committee in appropriate cases.

Fiduciary responsibility of controlling shareholders (relating to proposal 11.26)

We are supportive of the proposal to set out specific fiduciary responsibilities for controlling shareholders and also to consider the feasibility of requiring there to be a formal relationship agreement between the company and the controlling shareholder. This should be made available to minority shareholders to build their confidence, and it should specify the duties and responsibilities of the controlling shareholders.

Relations with shareholders (relating to proposal 11.30)

We firmly welcome SEBI's attention to the issue of the responsibility of shareholders, and the possibility of introducing an Indian stewardship code. We support the draft text of the code included in the consultation paper. We believe that this is an important step to addressing the occasional short-termism sometimes seen

in financial markets and is a further important step to increasing shareholder involvement with the aim of fostering sustainable long-term value creation and preservation. We are supportive of SEBI's request for mutual funds and asset managers to disclose their ownership policies and to become more active monitors and engagers with companies on matters of long-term value. It is important that an Indian Stewardship Code includes requiring institutional investors to publicly disclose their policies across all stewardship responsibilities. The ICGN's own Statement of Principles on Institutional Shareholder Responsibilities is attached; this is currently under review and a new version should be published in the middle of the year. We would be glad to discuss the details of this further with you.

It is hoped that through such a Stewardship Code the quality of the dialogue between investors and companies will be enhanced. The concept of actively monitoring investee companies through engagement is not widely practised in India; therefore a useful starting point would be for investors to establish guidelines regarding when they will actively intervene at a company to protect and enhance shareholder value.

If you would like to discuss any of these points, please do not hesitate to contact Kerrie Waring, ICGN Acting Head of Secretariat at +44 207 612 7079 or kerrie.waring@icgn.org. Thank you for your attention and we look forward to your response on the points above.

Yours sincerely,



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Co-Chair, ICGN Shareholder
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Co-Chair, ICGN Shareholder
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Michelle Edkins
Chairman of the ICGN Board of Governors

C c: ICGN Board Members
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