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SEBI'S CONSULTATION PAPER ON APPOINTMENT/ RE-APPOINTMENT OF MD/WTD IN THE LISTED SPACE

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INTRODUCTION

The Securities and Exchange Board of India (SEBI) issued a consultation paper on 27 January 2021 on the introduction of provisions relating to the appointment / re-appointment of persons who fail to get elected as Whole Time Directors (WTDs) / Managing Directors (MDs) at the general meeting of a listed entity. This has been done with a view to promoting corporate governance and upholding shareholder supremacy in the functioning of listed entities.

In common parlance, listed companies follow a practice of proposing 2 separate resolutions, (i) an ordinary resolution for the appointment as a director; and (ii) ordinary/special resolution for the appointment of WTDs / MDs. In this regard, there are no provisions under the law which restrict the listed entities from the appointment / re-appointment of WTDs/MDs whose candidature has once been rejected by the shareholders. The consultation paper seeks to address scenarios involving the appointment/reappointment of persons who fail to get elected as WTDs / MDs while proposing certain amendments to the SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015 (SEBI LODR).

BACKGROUND

Section 196 of the Companies Act 2013 (Companies Act), which pertains to the appointment of WTDs / MDs, states that such persons are appointed upon the approval of the board of directors at such terms and conditions including remuneration as the board deems fit. Further, such appointment is subject to the approval of the shareholders by a resolution at the next general meeting of the company.

However, the Companies Act does not explicitly prohibit the board from re-appointing a person as a WTD / MD, whose appointment to such posts was rejected by the shareholders at the general meeting. Hypothetically, the board of a listed entity can continue to appoint such persons as WTDs / MDs even after subsequent rejections by the shareholders. Such a situation becomes more likely in cases where a special resolution is required for appointment of WTDs / MDs whereas only an ordinary resolution was sufficient for the appointment of such person as a director. SEBI opines that such appointments by boards would go against the will of the shareholders and also against the spirit of corporate governance as envisaged under the SEBI LODR.

RECOMMENDATIONS / PROPOSED AMENDMENTS

In order to address situations of this nature, SEBI has proposed the following amendments to SEBI LODR:

- Re-appointment of such persons as WTDs/MDs who have been earlier rejected by the shareholders can only be made upon (a) recommendation by the Nomination and Remuneration Committee (NRC) along with detailed justification as to why such appointment is made and (b) approval of the board after recording reasons for such appointment.
- Additionally, upon appointment of such directors to the board, the listed entity shall be required to: (a) disclose reasons for such appointment to the stock exchanges within 24 hours along with the recommendation of the NRC (b) obtain shareholder approval for such appointment in the next general meeting or within 3 months, whichever is earlier and (c) provide detailed explanation from the NRC and the board to the shareholders for considering the appointment.
- Lastly, if the shareholders vote against the appointment of such persons again, a cooling off period of 2 years would be applicable during which they cannot be considered for appointment as director or continue as a director.

COMMENTS

SEBI's proposal can be seen in the context of rising shareholder activism leading to instances where appointment of key individuals as WTDs / MDs has been rejected by shareholders. With the increasing influence of proxy advisory firms over institutional shareholders, the number of such instances is expected to rise. It is not clear if any particular instance has led to the consideration of this proposal. However, as recently as in 2018, we witnessed the board of Apollo Tyres re-nominating Mr Neeraj Kanwar as a MD even after the shareholders rejected the same on grounds of high-compensation.

The proposal is a welcome policy intervention aimed at improving corporate governance in listed entities and attributing primacy to the shareholders. However, the wording of the proposed amendments raises certain doubts. It is ambiguous whether the latter part of the proposed amendments (as indicated at 3.2 and 3.3 above) applies in case of re-appointment of such persons only as WTDs / MDs or as ordinary directors also. A need for clarification is felt in this regard in order to avoid misinterpretation. The consultation paper is awaiting public comments to be accepted on or before 12 February 2021.

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