

**Review of the approval process for appointment and / or removal of Independent Directors - Amendments to the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015**

**1. Objective**

1.1. This memorandum seeks approval of the Board to amend regulation 25(2A) of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 (“**LODR Regulations**” / “**LODR**”) for insertion of a new optional provision relating to appointment of Independent Directors (IDs) and related provision for removal of Independent Directors in listed entities.

**2. Background**

2.1. The Companies Act, 2013 (“**Companies Act**”) has the following requirements with respect to appointment, re-appointment or removal of Independent Directors:

- a) Appointment of an Independent Director (1st term) to be approved by the shareholders through an ordinary resolution.
- b) Re-appointment of an Independent Director (2nd term) to be approved by the shareholders through a special resolution.
- c) Removal of an Independent Director appointed for the first term shall be through an ordinary resolution and removal of an Independent Director appointed for the second term shall be through a special resolution.

2.2. In order to strengthen the process of appointment, re-appointment or removal of Independent Directors and to limit the influence of promoters on the process by virtue of their shareholding, SEBI issued a consultation paper on March 1, 2021, proposing changes to the process of appointment, re-appointment or removal of Independent Directors at listed entities.

2.3. Based on the feedback received during the consultation process, the Board, in its meeting held on June 29, 2021, approved the proposal on appointment, re-appointment or removal of Independent Directors at listed entities by way of a

special resolution. Accordingly, a new sub-regulation i.e., regulation 25(2A) was interested in the LODR Regulations which became effective from January 1, 2022. The text of the sub-regulation is given below:

“The appointment, re-appointment or removal of an independent director of a listed entity, shall be subject to the approval of shareholders by way of a special resolution.”

### **3. Representations received**

3.1. Subsequent to the aforesaid amendment, SEBI received several representations on the revised requirement to appoint Independent Directors (1<sup>st</sup> term) through a special resolution. The representations inter-alia stated that in cases where there are multiple promoter groups holding substantial shareholding, appointment of an Independent Director may be opposed by one set of promoters due to internal disagreements with others, thereby rendering the proposed special resolution infructuous.

3.2. Therefore, the representations inter-alia suggested to consider an alternative for appointment of Independent Directors, which would require approval of all shareholders by simple majority along-with approval by simple majority of non-promoter shareholders i.e., “majority of minority”.

### **4. Need for an alternate method for appointment of Independent Directors**

4.1. The representations were examined in the light of the aforesaid challenges faced by some companies in appointing Independent Directors by way of a special resolution.

4.2. The suggestion to appoint Independent Directors through “majority of minority” may be considered as an alternate method for appointment of Independent Directors (in addition to the requirement of Ordinary Resolution for appointment in terms of the Companies Act) specifically for companies facing challenges in appointing Independent Directors through a special resolution. This would also be a positive step towards empowerment of the minority shareholders (i.e., public shareholders) as well.

4.3. The alternative method of appointment of independent directors, as proposed above, would work as follows:

In case a special resolution for appointment of an Independent Director does not get the requisite majority of votes, then the following thresholds would be tested:

- a) Whether the votes cast by all the shareholders in favour of the resolution is more than the votes cast against the resolution and,
- b) Whether the votes cast by the public shareholders in favour of the resolution is more than the votes, if any, cast by them against the resolution.

If the resolution crosses the above two thresholds, then such a resolution for appointment of the Independent Director would be deemed to be approved by shareholders. The aforesaid threshold will also be applicable for removal of such an Independent Director appointed under the alternate mechanism. This alternate method for appointment of Independent Directors is also easy to administer as the voting takes place only once.

4.4. This alternate mechanism for appointment and / or removal of Independent Directors was discussed in the meeting of the Primary Market Advisory Committee (PMAC) of SEBI held on August 4, 2022. After deliberations, the PMAC agreed with the proposal with a suggestion to clarify that removal of an Independent Director appointed for the second term shall be only through a special resolution, in line with the requirements under the Companies Act.

4.5. Based on the recommendations of the PMAC and the views expressed above, a summary of the requirements under the Companies Act, the LODR Regulations and the proposal to the Board is tabulated below:

Provision relating to	Companies Act, 2013	LODR Regulations (Regulation 25(2A)) (w.e.f. January 1, 2022)	Proposal to the Board (Amendment to regulation 25(2A) of the LODR Regulations)
Appointment of an Independent Director (1 <sup>st</sup> Term)	Ordinary Resolution	Special Resolution	Special Resolution. However, if the special resolution fails, Ordinary Resolution plus 'Majority of Minority'.
Re-appointment of an Independent Director (2 <sup>nd</sup> Term)	Special Resolution	Special Resolution	Please refer para 6.
Removal of an Independent Director	First term – Ordinary Resolution Second Term – Special Resolution	First term – Special Resolution Second Term – Special Resolution	<u>First term</u> <ul style="list-style-type: none"> <li>• If the Independent Director is appointed through a special resolution, removal shall be through special resolution.</li> <li>• If the Independent Director is appointed through ordinary resolution plus 'majority of minority', removal shall also be ordinary resolution and</li> </ul>

			<p>'majority of minority'.</p> <p><u>Second term</u></p> <p>Special Resolution (no change proposed).</p>
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## 5. Proposed amendments to the LODR Regulations

5.1. In order to give effect to the alternate mechanism for appointment or removal of Independent Directors, as discussed above, it is proposed to insert two provisos to regulation 25(2A) of the LODR Regulations. The proposed amendments to the LODR Regulations is placed as **Annexure** to the Board Memorandum.

## 6. Need for change in provisions relating to re-appointment of Independent Directors

6.1. The provisions relating to appointment, re-appointment and removal of Independent Directors as provided in the LODR Regulations are in addition to the requirements under the Companies Act. Therefore, amendments to the LODR Regulations should not be in conflict with the provisions of the Companies Act.

6.2. As the Companies Act requires special resolution for re-appointment of Independent Directors, no change is being proposed for re-appointment (and consequential removal) of Independent Directors in listed entities and the applicability of the alternate mechanism is limited only to appointment of Independent Directors (and consequential removal) in listed entities (1<sup>st</sup> term).

6.3. However, considering the benefits of the alternate mechanism as discussed at para 4.2 and 4.3 above and to ensure uniformity in the process of appointment, re-appointment and / or removal of Independent Directors, it is proposed to recommend to MCA to consider amendments to the Companies Act so as to

incorporate the aforementioned alternate mechanism for the purpose of re-appointment (and consequential removal as well) of Independent Directors, atleast for listed entities.

6.4. Accordingly, in addition to the existing requirement of special resolution, an additional provision for re-appointment (and consequential removal) of Independent directors in listed entities with the approval of simple majority of all shareholders and simple majority of public shareholders, in case special resolution fails, may be introduced in the Companies Act.

6.5. The aforesaid amendments to the Companies Act will facilitate SEBI to make suitable amendments to the LODR Regulations for introduction of the alternate mechanism for re-appointment (and consequential removal) of Independent Directors in listed entities on similar lines as that of appointment and / or removal of Independent Directors (1<sup>st</sup> term), as proposed in this Board Memorandum.

## **7. Proposal for consideration of the Board**

7.1. Considering that the alternate mechanism for appointment and / or removal of Independent Directors is a positive step towards empowerment of minority shareholders, the Board is requested to approve the proposed amendments to the LODR Regulations as mentioned at para 5.1 above. The Board is also requested to approve the proposals mentioned at paras 6.3 and 6.4 above on making recommendation to MCA for suitable amendments to the Companies Act.

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**Annexure**

(This shall be notified at a later date)