Volume 32, May 2024 ISSN 2581-5504

"Enhancing the Role of Independent Directors: A Comprehensive Analysis of Contribution Codes"

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Abstract

The present study 'Discipline of Independent Directors: 'Code to Contribution' focuses on the negative financial impacts of on board, remote board members and minimal or on-board involvement. By section 149(1) of Companies Act 2013, each organization generally must contain at least three numbers of members if is a public entity, two numbers of members if is a privately owned company and just one number of members if is a One Person Company. But however, it is being presence on Board and defining the financial performance of the company is a huge question. The reason the study is measured, thus, is to find the existence, independency and activities of Independent Directors and its effect on the financial success of the company.

Introduction

The Companies Act 2013 is the most important of its bills begetting the regulation and affairs' management of corporate entities in the Indian nation. Primarily, this action was initiated to repeal the previous Act as has been done in the year 1956. This repealing was in accordance with the aim to provide a new, efficient and advanced legal framework for a business entity operating in India. The Act sets out exacting guidelines on corporate governance, auditing, accountability and on Company directors' rights and causes and stakeholders' responsibilities. One salient thing that is seen in the Act, 2013 is that it implies the use of independent directors and their roles in boosting both integrity and quality of the corporate boards, this is mainly through the provisions relating to the appointments and roles of the independent directors. This part of the legislation makes sure that besides of making a profit, companies are accountable for their actions and behave in accordance with ethical governance, transparency principles, and a protection of stakeholders' interests. This provision establishes the standard for the whole companies' activities in the 21st century.[1]

Corporate governance frame involves an independent director to hold a crucial position and exhibit authority. With their directorates tasked to deal with the issues so that there are no conflicts of interest and nobody aiding or managing the company, the directors achieve that the company will follow the correct way that will have a benefit for shareholders, employees, customers, and the whole community. The critical function of the non-executive directors is to deliver impartial and objective assessment and supervision, minimizing the risk of the managing team using their authority inappropriately. Having placed in key committees, their

[1] "Independent Directors under Companies Act 2013" (*TaxGuru*, December 1, 2013) <https://taxguru.in/company-law/independent-directors-companies-act-2013.html> accessed May 2, 2024.

contribution in boardroom only emphasises how much power they have in reinforcing the corporate governance structure. The creation of good examples of governance integrity is made possible by the directors who maintain high standard accountability and integrity not only in the company but in general. This not only promotes the general principles of good governance but also significantly fortifies performance, stability and reputation in the long run. The procedures and complying with commands which has been laid in Act, 2013 are not like just a mere requirement but actually is a proper foundation on which the whole concept of corporate governance in India is built.[2]

Defining Independent Directors

The main objective of the policy under the Indian Companies Act, 2013, is to form a governance framework, by virtue of which the tasks and responsibilities of independent directors are critical and at the same time very precisely described. The Act imposes a universal obligation on all companies (Section 149(6)) that a non-executive director among others at the Board must be a person of integrity and have possession of necessary expert knowledge and experience. Besides, this defines directors to not qualify if they have any material pecuniary relationships or transactions with the company, its holdings, subsidiaries or associates in the company, or their promoters or directors. This also allows them to freely form opinions without any influence from the external factors. Accordingly, the company behaviours are determined based on fair judgment of these professionals.[3]

For a person to be an independent director, he/ she is required to meet several tough standards which emphasize their unbiased position and the fact that they are unaffiliated with management and major shareholders. Such criteria as absence of links to shareholders and members of the key managerial personnel both at the company (or companies) and its subsidiary, partners and associates are the basic requirements. Furthermore, they must not be the employees of the company or any group companies in any three consecutive financial years prior to the present year. Besides, there are limits in general on holding shares in a company and on cross-directorships which keep the independence of the organisations through and independent of the company management and the major stakeholders.

The differentiation of outside directors from other types of directors on the board is largely constructed on their roles and results on the board. The difference between the independent and the non-independent directors includes the fact that an executive director often bears more routine tasks and is involved in the day-to-day operations of the company, while the non-executive director takes part in the consulting process regarding policy making and strategic

[2] Wiersema M and Koo H, "Corporate Governance in Today's World: Looking Back and an Agenda for the Future" (2022) 20 Strategic Organization 786 <http://dx.doi.org/10.1177/14761270221115406>.
[3] "Companies Act, 2013 Key Highlights and Analysis" (*PwC*, November 30, 2013) <https://www.pwc.in/assets/pdfs/publications/2013/companies-act-2013-key-highlights-and-analysis.pdf> accessed May 2, 2024.

planning.[4] Nevertheless, independent directors' mission is to be objective in their points at the board meetings. This group perform an essential function by enabling senior executives to make decisions without prejudice and by touring to essential regulations and polices related to the business. Above that their atypical role allows them to view at the finance area from a different angle (best practices in governance, remuneration fairness, and financial reporting) concentrating on the specifics of their role and not connections to the company as in case with directors who are often biased in one way or another.

Roles and Responsibilities of Independent Directors

Independent directors act as an enormously effective instrument of corporate governance under the aegis of the Act, 2013. The Act has stipulated in a clear manner the roles of the Board of Directors in order to maintain impartiality in decision making of the management and ensuring that the management's decisions correspond to the best interests of all stakeholders including shareholders, workers, customers, and the community at large.

Independent director position is one of the mechanisms that act as sentinels of corporate integrity and is entrusted with obligations of supervision and strategic guidance. In India, an act mandates the inclusion of independent directors in board to ensure that the interests of all the shareholders are preserved from the biased approach by any particular individual having huge shares in the company. Enhancing the quality of board work and decision-making requires them to give a bold solution when addressing concerns both internally and externally because of their authority to do so without managerial influence.

The whole endeavour of the independent directors is to make the function of the board more transparent and democratic. They are the ones required to act as a security auditor within his company to avoid any misconduct or wrongdoing capable of diminishing public trust, as well as confidence from investors. This as inspection of the company's financial reports, judgment of its business processes, and confirming stated information by what organization has on the ground.[5]

The main mission of the imprudent directors is contributing and protection of the interests of all participants. It is their responsibility to make certain that an even-minded approach is applied by the board to decisions involving the impacts onto shareholders, their employees and all other entities affected. Such a balanced performance assists in absorbing fairness in

[4] Malhan Y, "Independent Directors- under the Companies Act, 2013" (*Lexology*, February 7, 2014) <https://www.lexology.com/library/detail.aspx?g=45f2cd2e-88a0-46bf-ba56-5b404c2e4681> accessed May 2, 2024.

[5] Mittal J, "Independent Director under Section 149(6) of Companies Act, 2013" (*TaxGuru*, November 10, 2022) <https://taxguru.in/company-law/independent-director-section-1496-companies-act-2013.html#:~:text=Schedule%20IV%20of%20the%20Companies%20Act%202013%20specifies,the%20company%20is%20following%20good%20governance%20policy%20.> accessed May 2, 2024.

 ISSN 2581-5504

operations, particularly where there is an overlap between a potential conflict of interest, and where shareholder activism is a prevalent factor.

They are responsible for supervision of accountancy processes through which external auditors are appointed and systems to systems of internal control and of reporting financial statements are monitored. They play a role of justice in formulating a standard remuneration package for the senior management as well as directors, in addition to creating a link to performance. They are among those who are involved in the process of nominating people to the board, giving attention to skills and experiences that are not only diverse but which are relevant to a board's optimal functioning. These committees further perform evaluation of the board's operations and the performances of individual board members.

Code of Conduct for Independent Directors

It is a part of the Companies Act, 2013, which is an act to provide and cultivate practice of good corporate governance among enterprises in India and encourages the growth in trust between businesses and stakeholders. Consequently, Schedule IV of the document imposes Code of Conduct that had been especially adapted for independent directors. The key element of the act requires operationalization of the mandate for independent directors, with a view to achieving forecasting and influential character, standards of business ethics and responsibility.[6]

Schedule IV gives a structured plan that points to ethics and professional standards that are the principles of independence directors. It comprises not only respect of the law requirements but also fortifies a certain attitude to the ethical issue solving and minds attitude to the sustainable firm development in general instead of mere observance of the legal requirements. The base on the assumption that is presented by the schedule consists of the general principles which are meant to guide the independent directors and includes guidelines on how they could avoid behaviour such as putting the needs of the shareholders and the company before their own, act objectively, and ensure that their decisions are not biased by personal interests.[7]

According to the Code of Conduct along with the fourth schedule, all duties and role of the independent directors are categorically listed. These sets of standards cover issues of conflict of interest, equality in the company's and consequently its shareholders' and other stakeholders' interests, and non-disclosure of sensitive information. Besides, the code involves disclosing the duties of independent directors to be upheld by them to promote transparency within the organization thus all disclosure should be based on facts and the implications reported to the board and shareholders. Besides, the mentioned code states that one of the independent directors' roles is to not only comply with the statutory regulations affecting the company but

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[6] "Roles And Responsibilities of Independent Directors Under Company Law" (*YLCC*, March 13, 2022) <https://www.yourlegalcareercoach.com/roles-and-responsibilities-of-independent-directors-under-company-law/> accessed May 2, 2024.

[7] "Schedule 4 of Companies Act, 2013 : Code for Independent Directors" (*Corporate Law Reporte*, April 30, 2024) <https://corporatelawreporter.com/companies_act/schedule-4-of-companies-act-2013-code-for-independent-directors/> accessed May 2, 2024.

also to carefully understand the business, as well as, its environment where the company is involved.

Schedule IV delineated the role of independent directors explicitly with the high quoted ethics and personal honesty. The directors are tasked with leadership of the company by directing it in the correct manner, though not engaging in acts that may be of benefit to them, but to the disadvantage of the company. Owing to it, they have to act as paragons of ethical leadership, putting the emphasis on the formation of compliance and ethics culture both in the officials and each employee. According to that, the role includes a supervisory function of the implementation of effective systems for internal control, risk management and public reporting. Besides, independent directors will serve as watchdog to the management and other board members to ensure that the operations of the company are alert, and if there is any untransparent action, they will challenge the officials of the company by working constructively.

Appointment and Tenure of Independent Directors

The structure of independent directors' vocation, permanency and tenure of term is central to the reputation of good and efficient governance within a corporation. In India, the general corporation law Act 2013 gives minute details of expected governance processes to produce complete transparency, independence, and necessity of specialized skills on board.

The whole endeavour is governed by the conjunctions of strict eligibility criteria and a formalized selection process. Under Section 149(6) of the Companies Act, 2013, independence of director is necessary for the extension of their work with company. Independent directors must be of trustworthiness and possess such characteristics like professionalism and experience. If any board members have any financial interests in the company, holding company, subsidiary or associate companies that may affect their independence, they should not be registered as a director or the board audit committee members. The process, however, is usually guided by the nomination and remuneration committee, which qualifies candidates for this position based on the array of factors including their verdict skills, business intuition and the type of the previous governance role.[8]

The second term which Mandatory requirement is strictly supervised by the Companies Act of Indian is the term of office of Independent directors. The tenure of independent directors chosen by the company shareholders is for not longer than of five years. However, the tenure can be more prolonged if a special meeting is held by the company to this effect and a report indicating this is included in the board's report in the following year. Subsequently, instead of an unrestricted period in the office, an independent director has only an option of holding his post for not more than two terms of 5 years each. After the first mandate is completed, the CEO

[8] "Clarifications Relating to Independent Directors "(*KPMG*, June 12, 2014) <https://assets.kpmg.com/content/dam/kpmg/pdf/2014/07/First%20Notes_12June14.pdf> accessed May 2, 2024.

should have a three-year-cooling-off period before being able to sit for the next CEO job in the same system. This provision is to ensure a proper distance and independent decisions are taken.

Based on their performance, evaluated in the process of an official, thorough review, independent directors may be reappointed or dismissal awarded. Evaluation of performance is the major task conducted by the board at least once in the year, which is discussed in the board meeting, whether it is conducted by the Nomination committee or any external organisation who is independent to insure the objectivity. The considerations for assessment such as the policy implementation, stakeholders' interests, and abode governance have also been made. The findings of the audits are always vital because they help the board of directors thus, they will determine whether to renew a director's term. A thorough measurement mechanism contributes not only for preserving or adding the performance of the ruling Board but it also consumes the responsibility of Independent Directors to the stakeholders they represent.

Challenges Faced by Independent Directors

The roles played by independents' directors are vital in the fact that they guide companies towards transparency and legitimacy. Unfortunately, those are also prone to several obstacles that disable them to perform effectively. Corruption is undoubtedly what comes into your head in the case of these perils. They manifest when personal preferences are contradicted with the responsibility that the mine owes to the company. The Companies Act of 2013 prescribes effective ways of dealing with conflicts of interest. It requires directors to inform the board on the matters that may be related to their personal interests, and avoid discussions and votes regarding which their interests are involved. These principles mark out the frameworks for this kind of disputes, but, in a more practical sense, meticulous monitoring and total devotion to the ethical norms are needed.

Rather, we are looking, frequently, to walk the thin line between what is required by law and what is prescribed by the statutes. Non-executive directors has to deal with the intricacy of the business governance and building the regulatory oversight compliance at the same time. This double-sided role contributes thus to a level of understanding that enables to engage in both the business's operational and size of the business does not reach a certain threshold and the customer's good is not in line with the expectations. Balancing act is very important, in which the current regulatory environment and emerging regulatory changes is vital for the continuous education and awareness raising of both traditional and future regulatory standards.

Conclusion

No doubt the work of independent directors is to be credited with making governance of the companies efficient and fair. They maintain the order through setting up a systematic program that is able to make sure corporations are not only playing by the law but also conducting their business activities in a well-grounded and morally upright manner. A proper enforcement of the code of contribution, as would be specified by the Indian Companies Act, 2013, will increase per unit company value and breeds stakeholder confidence. Through the objectivity exercising and impartiality in their work as independent directors, they ensure the company's management decisions align with the organizational long-term goals and the interests of stakeholders.

As the time goes by, and independence directors' responsibilities become more intricate and demanding, the role of independent directors is bound to change too. Being a flexible individual who is not only able to adopt and refine skill will be a necessity for the human resources managers working in the dynamic global business environment. Accordingly, their excursion is an unceasing process of acquiring new knowledge and evolution in their behaviour guided by principles of ethical leadership. In general, the principles of those independent directors must not be undermined (if not entirely by the companies they serve) for the overall economy, as it shall be proved to be more transparent, accountable, and sustainable by their contribution.