

# Ease of doing business: Functions of three committees can be performed by a single committee in unlisted public companies

*Dr S. Chandrasekaran*



The definition of a “public company” has been modified in the Companies Act, 2013 (the Act). In the earlier Act, it was defined in the main section, but now it is defined in the definition section itself. Now, even a private company which is a subsidiary of a public company and continues to be a private company in its articles of association shall be deemed to be a public company. Therefore, all such private companies necessarily have to comply with the provisions of the Act, as if such companies are public companies.

## **Constitution of Board of directors**

The minimum number of directors for a public company continues to be three. However, the Act imposed a condition of appointment of at least two independent directors for public companies:

- a) Having paid up share capital of ten crore rupees or more; or
- b) Having turnover of one hundred crore rupees or more; or
- c) Which have, in aggregate, outstanding loans, debentures and deposits exceeding fifty crore rupees.

The companies covered under above are required to appoint a higher number of independent directors; due to composition of audit committee, such higher number of independent directors shall be applicable for such companies.

## **Committees under the Act**

The Act has mandated four committees for unlisted public companies. One of the committees, namely, stakeholders relationship committee is to be constituted by a public company which consists of more than one thousand shareholders, debenture holders, deposit holders and any other security

holders at any time during a financial year. There are not many public companies that attract such constitution of stakeholders relationship committee.

The requirement of constitution of two other committees, namely, (a) audit committee and (b) nomination and remuneration committee, for public companies having paid up share capital and turnover are the same as that of the requirement of appointment of independent directors. In fact, the third condition attached is also almost the same except the one about borrowings for constitution of the said two committees.

Corporate social responsibility (CSR) committee is another requirement not only for public companies but also private companies.

### **Independent directors in committees**

All the above-discussed three committees mandate the appointment of independent directors in the following manner:

- CSR committee: Three or more directors, out of which at least one director shall be an independent director;
- Audit committee: Minimum of three directors with independent directors forming majority;
- Nomination and remuneration committee: Three or more non-executive directors out of which not less than one half shall be independent directors

### **Functions of the committees**

The Act has explicitly spelt out the function of the committees namely, the audit committee and nomination and remuneration committee. The functions of CSR committee have been provided in the Companies (Corporate Social Responsibility Policy) Rules, 2014. In all the committees, the appointment of independent director(s) is mandatory. In unlisted public companies, the shareholders are, normally, the family members, friends and relatives of directors. Some of the companies do have participation of banks and financial institutions and, to a certain extent, joint venture partners. Overall, the shareholders are known to the promoters and vice versa, and there is no public participation in such unlisted public companies.

### **Role of directors**

The directors are the promoters of the unlisted public companies. The capital employed is purely of that of the promoters. The working directors commonly belong to the promoters' group. Each and every director has to

take personal interest in the affairs of the company failing which their own capital will be at stake. The joint venture partners do involve in the day-to-day affairs of the company and their participation is also very much with that of the working directors. Banks and financial institutions also lend money, based on the credentials of the promoters. Overall, the role and functions of the directors in such unlisted public companies are just like that of the family members and friends. They have to be very careful in running the business not only to generate wealth for themselves but also to sustain in the long run.

### **Constitution of nomination and remuneration committee**

The basic requirement of constitution of this committee is to have a minimum of three directors who shall be non-executive directors. As discussed above, in unlisted public companies, the working directors are almost the promoters, joint venture partners and, therefore, in order to constitute a nomination and remuneration committee, such companies shall have to identify and induct in the Board at least three non-executive directors.

The functions of the said committee are to identify persons who are qualified to become directors and who may be appointed in senior management in accordance with the criteria laid down, recommend to the Board their appointment and removal, and carry out evaluation of every director's performance. One has to look into the past performance of all such unlisted public companies. Most of them exceptionally run well, and unless every promoter-director takes personal interest his own money would be at stake. The promoter-directors know by themselves whom to induct in the Board, whom to entrust with the senior management positions and so on; and now directing them to induct non-executive directors to constitute the committee to identify directors and senior management team is beyond one's imagination. The said committee would also formulate the criteria for determining qualifications, positive attributes and independence of a director and recommend to the Board a policy, relating to the remuneration for the directors, key managerial personnel and other employees; this is another issue which the promoter-directors are not interested to depend upon.

### **Three-in-one formula**

The audit committee members need to be financially literate. Corporate social responsibility functions also involve spending of the amount in the right direction within the parameters laid down in the Act and the Schedule drawn thereunder.

The number of independent directors in most of the companies is limited to two, just to comply with the provisions of the Act. The same two independent directors are part of the three committees to be mandatorily constituted by qualifying unlisted public companies. There is no additional brain involved in all the functions of the three committees and by constituting three different committees, it is only an added cost to the company by way of conducting the meetings, payment of sitting fees and so on, besides maintenance of registers and records. The role and function of nomination and remuneration committee of such unlisted public companies are very minimal since the appointment of directors in such companies is among the promoters and their relatives and friends who have financial stake in such companies. The role of CSR committee is also limited once the policy is formulated and projects are identified. At best, all the three committees can be clubbed into one committee of directors so as to give a fruitful meaning for constitution of such committee.

## **Conclusion**

The shareholders in a listed company are spread over globally and their interest is to be protected. Listed companies have to approve quarterly results. Promoters do pledge their shares and they have to honour their commitments. The provisions relating to insider trading, substantial acquisition of shares are to be complied with in letter and spirit to protect the interest of shareholders. Related party transactions are to be at arm's length and in the ordinary course of business. Any non-compliance or deviation would result in market speculation which would affect the shareholders interest. The number of independent directors is also more in listed companies and they can share their time and efforts in concentrating more in different committees in the overall interest of all stakeholders.

The shareholders in an unlisted public company are mostly the promoters and their friends and relatives. The promoters know how to protect their interest and if they fail in their duties, the end result would be disastrous for their wealth and growth.

The role and functions of three different committees are very limited in such unlisted public companies. The directors do not find any importance in all such meetings which would unnecessarily take out the time of the directors and increase the cost to the company. Single committee would take care of all the functions of all the three committees and this would not only reduce the cost to the companies but also avoid the precious time of independent directors.

*(Dr S. Chandrasekaran is Senior Partner, Chandrasekaran Associates, Delhi.)*