Listed Companies Disclosure: The Way Forward

Yogesh Dhingra
Chief Finance Officer & Chief Operating Officer
Blue Dart Express Ltd.

During recent times, "corporate governance" has gained significant attention and focus across the globe. Most evidently, the reason for this renewed focus has been a result of major corporate collapses and lack of governance standards.

In India, various initiatives have been undertaken in the past by the Ministry of Corporate Affairs (MOCA) and Securities & Exchange Board of India (SEBI) to ascertain that those entrusted with the responsibility of governing shareholder wealth are adequately regulated and made accountable. Over the past 15 years, there have been many reforms in the corporate governance framework - starting from constitution of the Kumar Mangalam Committee (1999), introduction of Clause 49 in the listing agreement (2000), revision in Clause 49 on recommendations of the Narayana Murthy Committee (2006), issue of voluntary guidelines on corporate governance (2009), issue of guiding principles on corporate governance (2012) based on recommendation of the Adi Godrej Committee, enactment of the revised Companies Act (2013) and finally the new corporate governance norms by SEBI (2014).

The concept of Corporate Governance in India gains importance from the following factors, which are time-tested and proven.

(a) Corporate governance is a must, not only to gain credibility and trust but also as a part of strategic management for survival, consolidation and growth.

(b) It explains the need to adhere to ethical business practices.

(c) Corporate governance strives to enhance Board Performance by emphasizing on the contributions of professionally qualified and experienced non-executive directors and Board Committees.

(d) Corporate governance strives to monitor and ensure absolute compliance with the laws of the land.

Although, the Companies Act 2013 specifies the minimum requirements of governance applicable to all companies, a recent press release by SEBI indicates a move towards aligning the requirement for listed companies with that of the Companies Act and simultaneously raises the bar on governance standards for listed companies.

The regulator has clearly indicated a move towards increased transparency on conducting Board matters and articulated several changes in the roles and responsibilities of the board, board committees and independent directors. The board of directors is a vital link between shareholders and management, and hence has a very critical role and responsibility in the overall governance framework. The Satyam episode has created an environment leading to serious discussions on corporate governance and the role of independent directors therein. Many opinions have been expressed in seminars, newspapers, magazines as well as in private discussions. The main theme is the role of independent directors in corporate governance. Independent directors can certainly contribute significantly towards enhanced Corporate governance.

The notification on Listing and Disclosure Regulations 2015 pertains to listing of different segments of the capital market and disclosure norms in relation to each of these segments. The latest set of norms provides broad principles for periodic disclosures by listed entities, apart from incorporating corporate governance principles. This announcement sought to streamline and enhance disclosure obligations of listed companies. The three different circulars briefly outline the following

Shareholder Voting Results

In the case of shareholders' meetings, SEBI has prescribed that a listed company must submit to the stock exchange the results of voting within 48 hours of the meeting. The details submitted must include the date of the meeting, the total number of shareholders as on the record date, and the numbers of those who attend in person or by proxy and those via video conferencing. The details should also include an agenda-wise break-up and whether a matter requires an ordinary resolution or special resolution.

More importantly, the total number of votes polled must be split into three categories, namely (i) promoter and promoter group, (ii) public institutions, and (iii) public non-institutions. This way, shareholders and the investing public will be clearly in a position to ascertain the manner in which votes were cast, and also the attitude of promoters as well as institutional shareholders. Since institutional shareholders are becoming more influential in the voting process, this disaggregated information will be helpful to investors. Another piece of information to be disclosed is whether the promoter or promoter group are interested in the agenda or resolution. This would become crucial in related party transactions as well as M&A deals between group companies. Overall, the transparency initiatives are welcome as it could help boost shareholder participation.

Business Responsibility Reporting

In addition to shareholder value, both the Companies Act as well as SEBI's regulations have focused on stakeholder responsibility. Until now, the reporting of these aspects was governed through the Government of India's "National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business". The reporting requirements have now been subsumed into the Listing Regulations, due to which SEBI has streamlined the disclosures as well.

SEBI's objectives are evident in its statement as follows: At a time and age when enterprises are increasingly seen as critical components of the social system, they are accountable not merely to their shareholders from a revenue and profitability perspective but also to the larger society which is also its stakeholder. Hence, adoption of responsible business practices in the interest of the social set –up and the environment are as vital as their financial and operational performance. This is all the more relevant for listed entities which, considering the fact that they have accessed funds from the public, have an element of public interest involved, and are obligated to make exhaustive continuous disclosures on a regular basis.

The disclosure requirements span a number of different aspects of social responsibility such as ethics, bribery and corruption, product matters, employment, human rights and the like. SEBI's circular also contains detailed Principles to Assess Compliance with Environmental, Social and Governance Norms.

Last year SEBI's Chairman, U K Sinha, also issued a stern warning to companies saying that the regulator and the exchanges are maintaining a strict vigil and the violators would not be spared. His primary concern was the transparency of corporate governance practices of companies investing in new companies. As per the latest World Bank report, India's ranking in investor protection has improved from 49 in 2012 to 34 in 2013 and now we are at seventh place. This means that India is ahead of some of the biggest markets in the world, and also one of the few countries where it has been mandatory that every listed company have one woman director on the board.

Reporting for IDRs

Listed companies with Indian Depository Receipts (IDRs) are required to file with the stock exchange the holding pattern of IDRs within 15 days of the end of each quarter. They are also required to submit to the stock exchange a comparative analysis of the corporate governance provisions that are applicable in its home country and in other jurisdictions in which its equity shares are listed along with the compliance of the same vis-à-vis the corporate governance requirements under the Listing Regulations. This will provide more information to investors regarding governance requirements and compliance. SEBI has also prescribed detailed procedures for two-way fungibility of IDRs.

Among the various disclosures requirements, those pertaining to IDRs may be least significant given that hardly any companies have made use of the market for IDR offerings.

Meanwhile, SEBI said norms with respect to allotment, refund and payment of interest, book closure date, requirement of one per cent security deposit, submitting multiple copies of documents to stock exchange, among others, may not be included in the new listing norms as they are either redundant or would be incorporated in a separate set of regulations.

Analysis

The 2015 Regulations became effective from December 1, 2015, with the exception of two regulations —Regulation 23(4) and Regulation 31A—that became effective on September 2, 2015, when the Regulations were notified. Regulation 23 deals with related party transactions, and sub-clause (4) of this regulation states that: "All material related party transactions shall require approval of the shareholders through resolution and the related parties shall abstain from voting on such resolutions whether the entity is a related party to the particular transaction or not."

The 2015 Regulations, in certain instances, moves beyond alignment with governance requirements and thresholds as provided under the 'Companies Act' and adopts a stricter approach towards the composition of the board, its committees and the duties of directors. It tends to retain the higher requirements of Clause 49 of the equity listing agreement as well as amends some of the voluntary guidelines, to make them mandatory.

For instance, as per the Companies Act, at least 1/3rd of the board of directors of a listed company must comprise of independent directors. However, Regulation 17 retains the earlier threshold requiring 50% of the board to be independent, if the chairperson is not a non-executive director. Similarly, while the Companies Act requires that audit committee members must be financially literate (i.e. capable of reading and understanding financial statements), Regulation 18(1)(c) maintains the mandate of having at least one member who possesses "accounting or related financial management expertise".

Further, it also retains the requirement of valid quorum of at least two independent directors for conducting an audit committee meeting, thereby making it indirectly imperative for all listed companies to appoint at least two independent directors. The 2015 Regulations also provide for constitution of "risk management committee" for top 100 listed entities determined on the basis of market capitalization at the end of previous financial year. Earlier, the listing agreement merely mandated the board to inform shareholders regarding risk assessment and minimization procedures adopted for the same without a requirement of a specific committee as such. Furthermore, constitution of remuneration committee and framing of whistleblower policy are now made mandatory compliances as opposed to voluntary practices under the listing agreement. Additionally, Regulation 46 requires disclosure

of composition of various board committees on company's website.

In August 2015, SEBI changed the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 to enable listing of certain categories of start-ups without undergoing an initial public offer. The underlying objective was to liberalise the stricter listing compliances and de-incentivize start-ups opting to list on foreign stock exchanges. These start-ups must alter their structure into public companies prior to listing. Further, they can raise capital only through rights issue and private placement (which were otherwise available under Companies Act) and cannot invite retail investments or make any public offer. SEBI's model agreement for listing on the institutional trading platform did not relax the start-ups from complying with the corporate governance requirements as contained in the Companies Act. For instance, a listed start-up has to necessarily appoint 1/3rd of its board with independent directors, appoint 1 woman director, constitute board committees, set up vigil mechanism and put in place various internal controls and systems. Compliance with corporate governance provisions involves structural and compliance costs, substantial time for a start-up and continues to act as a deterrent for listing, despite floating of the alternative mechanism.

Looking Ahead

The 2015 regulations were put into effect with an aim to allaying the provisions of listing agreements with the provisions of Companies Act, 2013 and thereby enforcing better corporate governance and disclosure requirements. Earlier, a listing agreement was the agreement between the relevant stock exchange, and a listed company, whereby the listed company agreed to comply with the provisions of the listing agreement and, so, it didn't enjoy statutory recognition.

However, Section 21 of the Securities Contract Regulation Act, 1956, proclaimed – "Where securities are listed on the application of any person in any recognised stock exchange, such a person shall comply with the conditions of the listing agreement with the stock exchange". Hence the listing agreement got statutory enforceability but there was no separate regulation through which the obligations cast by the stock exchange were regulated. Also there were different listing agreements for debt and equity and different regulations for different classes of securities. SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 enables SEBI to directly regulate and obligate listed entities to comply with the provisions of SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015.

Contravention of the 2015 Regulations will result in imposition of fines, suspension of trading, freezing of promoter or promoter group shares, or any other action as SEBI may deem fit. Further, the 2015 Regulations gives statutory status to the contractual clauses of listing agreements and, by extension, breach of the 2015 Regulations will invoke penalty clauses under the SEBI Act.

These regulations have caused mixed reactions. Some perceive the clauses as "old wine in a new bottle" while some are concerned about the method of their implementation. As discussed above, the new regulations retain stricter standards than the Companies Act in order to promote governance of listed entities and protect investor interests. The 2015 Regulations have adopted a unilateral approach for all kinds of businesses and their enthusiasm to ensure ethical conduct has resulted in some level of disconnect with business realities.

The timely compliances will involve cost and resources for listed entities and may cause difficulties in implementation for medium and small companies. This makes the 90-day time period fairly critical for listed companies to assess their preparedness for ensuring compliance and avoiding hefty penalties.

Through the Listing Regulations SEBI seems to have made a sincere effort to consolidate the different listing agreements pertaining to various securities under Capital Markets and bringing them under one umbrella regulation and also getting statutory recognition and enforceability through the regulations. It's still early days to comment on the success of last year's notification and take stock of how the regulator has benefitted. Either way the people most impacted by this Act have been secretaries as the listed firms — the people saddled with the responsibility of ensuring compliance!