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INDEPENDENT DIRECTORS AND CORPORATE GOVERNANCE IN INDIA: ROLE, RESPONSIBILITIES AND CHALLENGES

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Abstract

Indian boards are rarely meetings of equals. In most of the listed companies a promoter family or group holds a controlling stake, and the directors who sit beside it were often introduced by it. Independent directors are the law's answer to that imbalance: outsiders who are meant to examine proposals without a stake in the outcome, and to speak for shareholders who have no seat of their own. This article looks at how the idea has been built into Indian law through the Companies Act, 2013 and the SEBI Listing Regulations, what those instruments ask of independent directors and what they give in return by way of a qualified shield against liability, and how the Supreme Court has approached the personal responsibility of directors. It then asks why the formal structure has not always produced real independence, pointing to promoter influence over selection, dependence on management for information, the economics of the role, and board cultures that can treat dissent as disloyalty. The article closes with reform proposals aimed less at adding rules than at changing who selects, informs and protects these directors. Its central claim is that independence should be tested by what a director can actually do in a meeting, not by how many appear on a board list.

Keywords: independent directors; corporate governance; Companies Act, 2013; SEBI Listing Regulations; promoter control; minority shareholders; director liability.

1. Introduction

Picture a board meeting at a promoter-led company. The papers reached the directors the evening before. The chairman has already spoken to most of the room. Item seven of eleven is

a loan to a group company, and it passes in two minutes because the people who might object either owe their seats to the promoter or have not had time to read the numbers. This is an illustration, not a report on any particular firm, but it describes a risk that Indian company law has been trying to design out for more than two decades.

The legal device is the independent director: a non-executive member of the board with no material tie to the promoters or the management, appointed to bring detached judgment to the table and to look after shareholders who have no seat of their own. Indian law now makes such directors compulsory for listed companies and for larger public companies, and it surrounds them with eligibility conditions, term limits, a code of conduct, committee responsibilities and a qualified shield against personal liability.

This article asks how well that design works. Its argument is easy to state. Independence is not a status that a statute can confer on a person; it is a capacity that a director either has or lacks at the moment a controversial proposal is on the table. That capacity depends on four things the law only partly controls: who chooses the director, what the director is told, what the director stands to lose by objecting, and whether the room tolerates objection. The sections that follow keep returning to those four questions.

Part 2 explains why Indian boards need outsiders in the first place, and Part 3 traces how the present law developed. Part 4 sets out who qualifies as independent and how appointment, tenure and pay are regulated, while Part 5 describes what these directors are expected to do. Part 6 turns to personal exposure and reads section 149(12) of the Companies Act alongside four Supreme Court decisions. Part 7 looks at why formal independence often falls short, Part 8 offers reform proposals, and Part 9 concludes.

The method is doctrinal. The primary materials are the Companies Act, 2013, the rules made under it, the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (the "Listing Regulations") and decisions of the Supreme Court of India; committee reports and commentary supply the background. The law is stated as it stood in November 2026. SEBI amends the Listing Regulations often, so any threshold mentioned below should be checked against the current consolidated text before it is relied on.

2. Why Boards Need Outsiders

The classic account of corporate governance worries about managers who spend other people's money. Shareholders are scattered, managers are informed and present, and the board is supposed to stand between the two. That account fits widely held companies well, but it is only half the Indian story.

Many Indian companies, listed ones included, are controlled by a promoter or promoter group holding a block of shares large enough to carry most ordinary resolutions alone. The promoter frequently chairs the board, or a relative does, or the managing director is a nominee. In that setting the sharper conflict is not between owners and hired managers but between the controlling shareholder and everyone else. The temptations are familiar: related-party contracts on generous terms, intra-group loans and guarantees, asset transfers at convenient prices, and remuneration that bears little relation to performance. None of these needs to be hidden from a board that the controller has chosen.

An independent director is meant to be the one member whose seat the controller did not, or at least did not entirely, arrange. The role is protective and, in a measured sense, adversarial: to ask for the valuation report, to question the pricing, to insist that the minutes record a doubt. The idea is easy to caricature. Independent directors are not meant to run the business, and they are not meant to oppose management out of habit. What they supply is a credible possibility that a bad proposal will meet resistance, which is often enough to stop it being brought forward at all.

That deterrent function explains why the Indian debate keeps returning to the quality of independence rather than the number of independent directors. A board can be one-third or one-half independent on paper and still offer the promoter no resistance whatever.

3. How the Law Developed

Before 2013 the category barely existed in company statute. The Companies Act, 1956 said nothing about independent directors; the idea entered Indian practice through the stock exchanges. After the report of the Kumar Mangalam Birla Committee, SEBI introduced Clause 49 into the listing agreement in 2000, requiring listed companies to maintain a minimum share of non-executive and independent directors and to constitute audit committees. The N R

Narayana Murthy Committee later pushed the standards further. This was governance by contract with the exchange, and its enforcement was correspondingly limited.

Satyam changed the tone of the conversation. In January 2009 the company's founder-chairman wrote to his board admitting that the accounts had been inflated for years. The company had an audit committee and independent directors, and that was precisely the uncomfortable point: the machinery of oversight was present and had not caught the problem. The episode is widely cited as one of the pressures behind the governance provisions of the Companies Act, 2013.

The 2013 Act then did what the listing agreement could not. It defined the independent director in statute, fixed minimum numbers, created a databank of eligible candidates, annexed a Code for Independent Directors as Schedule IV, limited tenure and, importantly, wrote a limit on personal liability into the same section that set out the director's obligations. The Listing Regulations, which replaced the old listing agreement in 2015, repeated and tightened these rules for listed companies.

The Kotak Committee report of 2017 and a series of SEBI amendments since have shifted the focus from how many independent directors a company has to how they are chosen, paid, supported and removed. Appointment and removal of an independent director of a listed company now needs a special resolution, with a fallback that looks to the votes of public shareholders where the special resolution falls short; the circumstances of a resignation must be disclosed in some detail; and larger companies are expected to insure their independent directors. The direction of travel is consistent. The law has stopped assuming that independence follows from eligibility criteria and has started regulating the conditions in which independence is exercised.

4. Who Counts as Independent

4.1 The statutory test

The definition in section 149(6) of the Companies Act works in two layers. The first is a positive standard: the person must be, in the board's opinion, a person of integrity with relevant expertise and experience. The second is a catalogue of disqualifying ties. An independent director cannot be a managing director, whole-time director or nominee director, cannot be a

promoter or related to one, and cannot have had a pecuniary relationship with the company, its holding, subsidiary or associate companies, or their promoters and directors during the two preceding financial years or the current one. Dealings by close relatives are caught as well. Employment or key managerial office in the group within the previous three financial years disqualifies, as does a recent association with the company's auditors, legal advisers or consultants, a holding of two per cent or more of the voting power, and certain leadership roles in non-profit bodies that depend on the company or its promoters.

Two features stand out. The test is largely about money and kinship, which can be measured. And the one element that cannot be measured, integrity and expertise, is judged by the very board that the candidate is about to join. Part 7 returns to that soft spot.

4.2 Numbers

The numbers are set in several places. Every listed public company must have at least one-third of its board made up of independent directors, and prescribed classes of public companies, defined by paid-up capital, turnover or borrowings, must have at least two. For listed entities the Listing Regulations go further: one-third if the chairperson is a non-executive director, and one-half if the chairperson is an executive, or is a promoter or related to one.

4.3 Appointment

Appointment is meant to be independent of management. The Act provides for a databank of eligible persons, maintained under section 150 and the 2014 Rules, and candidates who are not exempt by virtue of experience must clear an online proficiency test to stay on it. The databank is a convenience, not a vetting service: responsibility for due diligence rests with the company making the appointment. Each independent director must give a declaration of independence at the first board meeting after appointment, again every financial year, and again when circumstances change. Schedule IV adds that selection should be independent of management and that the appointment should be made by a formal letter setting out the terms, the time commitment expected and the director's duties, open for inspection by members.

4.4 Tenure and pay

Tenure is capped. An independent director holds office for up to five consecutive years, may be reappointed once for a further term of up to five years by special resolution, and after two

terms must stay away for three years, during which he or she may not be associated with the company in any other capacity either. Independent directors do not retire by rotation.

Pay is deliberately modest in structure. An independent director may receive sitting fees, reimbursement of expenses and, if members approve, a profit-related commission, but may not receive stock options. The logic is plain: remove the incentive to tie one's own fortunes to a share price that management influences. The side effect is that the director has little financial reason to take on the company's controversies and, as Part 6 shows, a fair amount of financial and reputational reason to avoid them.

5. What the Law Asks Them to Do

Schedule IV is the closest the Act comes to a job description. Part II sets out the role: to bring independent judgment to strategy, performance, risk management, resources, key appointments and standards of conduct; to scrutinise management's performance against agreed goals; to satisfy themselves about the integrity of financial information and the strength of financial controls and risk systems; and to safeguard stakeholders' interests, particularly those of minority shareholders. A line that is easy to skim past asks them to moderate and arbitrate where the interests of management and shareholders conflict.

Part III turns the role into conduct. Directors are to undergo induction, keep their knowledge current, seek clarification and, where necessary, take outside professional advice at the company's expense. They are to attend and take part constructively in meetings and, where they have concerns about the running of the company or a proposed action that remain unresolved, to insist that those concerns are recorded in the minutes. They are to satisfy themselves that the vigilance mechanism works and to report suspected fraud or unethical conduct. Two of these matter for what follows: the right to outside advice at the company's cost, and the duty to have unresolved concerns minuted. They are the ordinary tools by which an independent director can both act and prove that he or she acted.

Schedule IV also requires the independent directors to meet separately at least once a year, without non-independent directors or management, to review the performance of those directors and of the chairperson and to assess the quality, quantity and timeliness of the information reaching the board. Separately, the performance of each independent director is

evaluated by the whole board, excluding the director under review, and that evaluation feeds into the decision whether to extend the term. Part 7 explains why this last feature is troublesome.

Much of the day-to-day work happens in committees. The audit committee must have a majority of independent directors under the Act; under the Listing Regulations at least two-thirds of its members must be independent, with an independent director in the chair. The nomination and remuneration committee also leans heavily on independent members, and larger companies must have a stakeholders relationship committee chaired by a non-executive director.The audit committee's functions include scrutiny of inter-corporate loans and investments, valuation of assets and undertakings, and evaluation of internal financial controls. Under the amended Listing Regulations only the independent members of the audit committee vote on related party transactions. This is probably the most concrete way in which the law gives independent directors something they can actually refuse.

Other provisions extend the reach. A listed company must have at least one of its independent directors on the board of each material unlisted subsidiary, so that governance does not stop at the front door of the group. A person may serve as an independent director in no more than seven listed entities, and in no more than three if he or she is a managing or whole-time director of any listed entity. Companies must also run familiarisation programmes for their independent directors.

6. Exposure and Protection

The same Act that gives independent directors their work also exposes them to personal liability for doing it badly. Section 166 applies to every director. It requires a director to act in good faith to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, shareholders, the community and the environment; to exercise duties with due and reasonable care, skill and diligence and to bring independent judgment to bear; to avoid situations of conflict; and not to make or attempt undue gain. A contravention carries a fine of between one lakh and five lakh rupees, and breach of the underlying fiduciary duties can found other proceedings as well.

Because independent directors do not run the company, applying the same exposure to them as to executives would be unfair and, in practice, would empty the boardroom of the people the law wants there. Section 149(12) therefore limits the liability of independent directors, and of non-executive directors who are neither promoters nor key managerial personnel. They answer only for acts or omissions of the company that occurred with their knowledge, attributable through board processes, and with their consent or connivance, or where they did not act diligently.

The phrase "attributable through board processes" repays attention. A fair reading is that it ties a director's knowledge to what the board's machinery actually put in front of that director: the agenda papers, the minutes, the committee reports. A director who reads the papers, asks the question and has the dissent minuted has a record that answers the knowledge and diligence limbs together. A director who skips meetings or signs without reading has handed an investigator a different argument. Seen this way, section 149(12) is not a free pass; it converts good practice into a legal defence. It is also a defence that has to be raised once proceedings have begun, which is where much of the practical anxiety lies.

Section 149(12) is comparatively recent, and the decisions discussed below arose before it or under other statutes. None of them involved an independent director under the 2013 Act, so they are best read as indicators of judicial attitude rather than direct authority. Four are worth setting side by side.

Official Liquidator, Supreme Bank Ltd v P A Tendolkar arose from misfeasance proceedings against the directors, managing director and officers of a bank in liquidation. The Court did not treat the board as one undifferentiated body. It looked at what each director had done or failed to do, and it held some directors jointly and severally liable with the managing director for part of the loss. The case is commonly cited for the proposition that gross negligence in supervision, and not only active wrongdoing, can ground liability, and that a director cannot escape by delegating everything to others. Its limits matter as well: the proceedings were under the Companies Act, 1913 and the Banking Companies Act, 1949, and liability turned on the individual's own part in the loss.

N Narayanan v Adjudicating Officer, SEBI concerned a whole-time director of Pyramid Saimira Theatre Ltd who was penalised for market abuse under the SEBI Act and the Prohibition of Fraudulent and Unfair Trade Practices Regulations. The Supreme Court upheld the penalty and spoke strongly about market integrity, noting that directors and insiders of listed companies are expected to use their powers with the utmost care, skill and diligence. The appellant was an executive, so the decision does not speak to independent directors directly. It does show the standard of conduct the Court expects of those who sit inside a listed company.

Sunil Bharti Mittal v Central Bureau of Investigation deals with criminal responsibility. The Special Judge had summoned senior figures in the telecom companies on the footing that, as the companies' directing minds, the companies' alleged offence could be attributed to them. The Supreme Court set the summons aside. The alter ego principle, it explained, attributes the guilt of those who control a company to the company, not the other way round. A director does not become criminally liable merely because the company is accused: vicarious liability needs a statutory basis, and without one an individual can be made an accused only if there is sufficient material showing his or her own active role coupled with criminal intent. The decision is among the strongest authorities for the proposition that a seat on the board is not proof of participation.

Pooja Ravinder Devidasani v State of Maharashtra applied the same instinct to section 141 of the Negotiable Instruments Act, 1881. The Court recognised that a non-executive director is ordinarily not involved in the day-to-day running of the company's business, and it quashed proceedings against the appellant because the complaint did not make specific averments that she was in charge of, and responsible to the company for, the conduct of that business. Being connected to a company in some way, the Court indicated, does not by itself bring a person within the provision.

Read together, the cases point the same way: courts look at role and conduct rather than title. That should reassure a careful independent director and warn a careless one. It also exposes the difficulty from the director's side. The protection arrives at the end of a process whose early stages, an investigation or a summons, can be damaging whatever the final outcome.

7. Why Independence on Paper Falls Short

Satyam was the first public reminder that the machinery of oversight could be present and still fail. The collapse of IL&FS in 2018 raised the question again for a sprawling group, whose many directors, independent and nominee alike, saw their knowledge and diligence examined in public. Each of the four questions posed at the outset produces a weak point.

7.1 Who chooses

The nomination committee proposes, the board recommends and the general meeting approves. In a promoter-controlled company that chain runs back to the promoter at every link. The special resolution rule and its fallback give public shareholders a say in ratifying or blocking an appointment; they do not give them a hand in choosing the candidate, who is still found through the company's own network. And the assessment of integrity and expertise remains the board's own opinion. A person can therefore meet every statutory criterion and still owe the seat to the promoter's goodwill, a debt that no disclosure form records.

7.2 What the director is told

An independent director sees the company through documents prepared by management. Late agendas, summary papers in place of source documents and items tabled on the day are the classic ways of informing a board without enlightening it. Schedule IV gives the independent directors' separate meeting the job of assessing information flow, and it permits outside advice at the company's expense, yet both depend on the director knowing what to ask for. The secretarial standard on board meetings contemplates seven days' notice of a meeting along with the agenda and notes, and a practice of routinely falling short of that is a concern worth recording.

7.3 What the director stands to lose

Objecting has a price. The second term depends on an evaluation by the board and on a shareholder vote that the promoter dominates, so the first term carries an incentive to be agreeable. Fees are modest and cannot be supplemented with options. Exposure to investigation, even if ultimately unfounded, is real, and insurance is mandated only for certain classes of listed entity and usually excludes deliberate wrongdoing. A director with a busy professional practice and several board seats may reasonably calculate that a public dispute

will cost more than it protects. The last resort left is resignation. The reasons for an independent director's resignation must now be disclosed, which turns resignation into a signal, but it is a signal sent from outside the room after the argument has been lost.

Time is a related constraint. The cap of seven listed-company directorships assumes that one person can prepare seriously for seven sets of board and committee papers. It is a ceiling, not a recommendation, and a director who treats it as an entitlement risks becoming a signatory rather than a supervisor.

7.4 Whether the room tolerates objection

Culture does what rules cannot. In a board where the chairman's preference is understood in advance, a question can sound like an accusation and a minuted reservation can sound like disloyalty. Directors then learn to raise concerns informally before the meeting, if at all, which leaves no record and applies no pressure. Whether a board treats disagreement as part of the job is a matter of habit, set by the chair and by the first few occasions on which somebody says no.

7.5 Compliance as the goal

Compliance can become the objective instead of the means. Diversity rules, including the requirement that larger listed companies have at least one woman independent director, widen the pool, but a seat given for compliance without a real voice adds little. The same goes for expertise. A well-qualified generalist may struggle to test the assumptions of a technology, financial services or infrastructure business, and the committee system then concentrates the burden on whichever director happens to understand the accounts.

8. Reform Proposals

The proposals below do not lengthen the rulebook. They are aimed at the four questions: who chooses, what the director is told, what the director risks, and what the room tolerates. They are the author's suggestions and several would need amendment of the Act or the Listing Regulations.

Selection the promoter cannot steer. The databank and special resolution rules can be taken further. A nomination committee made up mostly of independent directors could be required

to publish the criteria it applied and the number of candidates it considered, and public shareholders could be given a distinct approval step for appointment, in the way related party transactions are already ring-fenced. A lead independent director, chosen by the independent directors themselves, would give outside shareholders and regulators a named person to turn to.

An information right with teeth. The Schedule IV right to outside advice should be paired with a duty on the company to supply the documents an independent director asks for within a fixed period. The annual report could carry a short statement of how often independent directors sought additional information and what followed. Chronic late tabling of board papers should be reported to the independent directors' separate meeting as a governance matter, not left as a scheduling inconvenience.

Evaluation that does not depend on the people being supervised. At present independent directors are evaluated by the whole board, and the result informs reappointment. A better design would assign that evaluation to the independent directors' own meeting, with periodic external review, and treat the views of promoter-appointed directors as input rather than verdict.

Rethinking the second term. A single, longer, non-renewable term, of seven years for example, would remove the most obvious source of pressure. The cost is lost continuity, which could be softened by staggering terms so that a board never loses all its experienced independent directors at once. This is a trade-off, and reasonable people could prefer the present structure with a stronger evaluation process. What is hard to defend is the present combination, in which a director's renewal rests on the goodwill of those being supervised.

Making section 149(12) work early. Regulators and investigating agencies could adopt published guidance that, before an independent director is named in a complaint or summons, the record of board processes (attendance, papers circulated, minutes, recorded dissent) is examined. That would not shelter wrongdoers. It would insist that the question the statute asks, namely knowledge, consent or want of diligence, is asked first.

Support in proportion to risk. Insurance could be extended beyond the largest companies, and induction should include a working session on the company's main risks, related-party exposures and control weaknesses, in place of a general lecture on duties.

Making dissent ordinary. Chairs should treat a minuted reservation as a normal event. Companies might consider telling shareholders, in summary form, how many reservations independent directors recorded in a year. Counting reservations as a sign of health rather than discord would, over time, change what directors feel safe saying.

9. Conclusion

Independent directors were brought into Indian law to answer a specific problem: boards controlled by the people they are meant to supervise. The Companies Act, 2013 and the Listing Regulations have built a detailed structure around the answer, with definitions, quotas, a databank, a code, committee roles and a qualified shield against personal liability. That structure is valuable and, in many places, carefully drafted.

What it cannot do alone is create the willingness to say no. That depends on who selects the director, what the director is shown, what objecting costs and whether the board's culture can bear it. Where those conditions are weak, the one-third or one-half of the board listed as independent in an annual report is a figure and not a safeguard. The next stage of reform should therefore concern itself less with counting independent directors and more with the conditions in which they can do their job. A useful test for any proposal is whether it would make it easier for an independent director to ask an awkward question, to get a straight answer, and to be left unpunished for having asked.

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