

**THIRTY-SIXTH REPORT
COMMITTEE ON PUBLIC
UNDERTAKINGS
(1987-88)**

(EIGHTH LOK SABHA)

**NOMINATION OF DIRECTORS BY FINANCIAL
INSTITUTIONS
(Ministry of Finance, Department of Economic Affairs)**

**[Action taken by Government on the recommendations contained in
the 27th Report of the Committee on Public Undertakings (Eighth
Lok Sabha)]**



Presented to Lok Sabha on 25 February 1988

Laid in Rajya Sabha on 25 February 1988

**LOK SABHA SECRETARIAT
NEW DELHI**

February, 1988/Magha 1909(s)

Price : Rs. 17.00

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COMMITTEE ON PUBLIC UNDERTAKINGS
(1987-88)

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**ACTION TAKEN SUB-COMMITTEE OF THE COMMITTEE ON
PUBLIC UNDERTAKINGS**

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3. Shri K. P. Singh Deo
4. Shri Dinesh Goswami
5. Shri Zainul Basher
6. Prof. P. J. Kurien
7. Prof. Saif-ud-din Soz

INTRODUCTION

I, the Chairman Committee on Public Undertakings having been authorised by the Committee to submit the Report on their behalf, present this 36th Report on Action Taken by Government on the recommendations contained in the 27th Report of the Committee on Public Undertakings (Eighth Lok Sabha) on Nomination of Directors by Financial Institutions.

2. The 27th Report of the Committee on Public Undertakings was presented to Lok Sabha on 29 April, 1987. Replies of Government to all the recommendations contained in the Report were received on 30 November, 1987. The replies of Government were considered by the Action Taken Sub-Committee of Committee on Public Undertakings on 20 January, 1988. The Committee also considered and adopted this Report at their sitting held on 20 January, 1988.

3. An analysis of the action taken by Government on the recommendations contained in the 27th Report (1986-87) of the Committee is given in Appendix II.

VAKKOM PURUSHOTHAMAN

Chairman,

Committee on Public Undertakings.

NEW DELHI;

February, 18, 1988

Magha 29, 1909 (S).

CHAPTER I

REPORT

The Report of the Committee deals with the action taken by Government on the recommendations contained in the Twenty Seventh (Eighth Lok Sabha) of the Committee on Public Undertakings on 'Nomination of Directors by Financial Institutions' which was presented to Lok Sabha on 29 April, 1987.

2. Action Taken Notes have been received from Government in respect of all the 20 recommendations contained in the Report. These have been categorised as follows:—

(i) *Recommendations/Observations that have been accepted by Government.*

S. Nos. 1—11, 13—19.

(ii) *Recommendation/Observation which the Committee do not desire to pursue in view of Government's reply:*

—Nil— ..

(iii) *Recommendation/Observation in respect of which reply of Government has not been accepted by the Committee.*

S. No. 12

(vi) *Recommendation/Observation in respect of which final reply of Government is still awaited.*

S. No. 20.

3. The Committee desire that the final reply in respect of recommendation for which only interim reply has been given by Government should be furnished to the Committee expeditiously.

4. The Committee will now deal with the action taken by Government on some of their recommendations.

A. Follow-up action on recommendations

Recommendation S. Nos. 2, 9, 14 and 17, Paragraphs 2.2, 2.9, 2.14 and 2.17

5. In response to the Committee's recommendations for strengthen the financial institutions, the Government is reported to have issued instructions to the financial institutions to implement the recommendations of the Committee. For instance in regard to

appointment of nominee directors in all assisted companies, the Government have stated that institutions will soon review the position with reference to the latest list of assisted companies and appoint nominees, where necessary. Similarly in regard to recommendation of the Committee for strengthening the cadre of official nominee directors, it has been stated that IDBI has reported that the cadre of official nominees is being strengthened by the institutions. For yet another recommendation for undertaking a review to pin-point the shortcomings in the present system of working of nominee directors, it has been stated that Government have advised the institutions to have six monthly periodic review of the system of nominee directors including their performance in general and brought up before the Board of the concerned institutions for their constitution.

6. The Committee are glad to note that Government has accepted the recommendations of the Committee and financial institutions have been given necessary instructions to act accordingly. However, the Committee desire that the Government should further pursue the matter with respective financial institutions with a view to ensuring that the recommendations made by the Committee in regard to appointment of nominee directors should be implemented in letter and spirit and if necessary a time bound schedule should be prepared for the institutions.

B. Nominee Directors Cell

Recommendation S. No. 12, Paragraph 2.12

7. The Committee had noted that financial institutions has set up Nominee Directors' Cell and the Officers attached to these cells, who function only as nominee directors, were being appointed on each of as many as 15 Companies. The Committee had felt that an officer would not be able to do full justice if he was on the boards of 15 companies at a time. The Committee accordingly recommended that the number of nominations should be restricted maximum to not more than eight or ten companies and the Nominee Directors' Cell should be strengthened accordingly.

8. In their reply the Government have stated that Instructions have been issued by Government to make an evaluation of the performance of these Cells to see how the constitutions of the Cells in the institutions have improved the effectiveness and functioning of the nominee directors of the institutions on the Board of assisted companies. Institutions are reported to have been asked to make a review of the functioning of these Cells and the matter would also be reviewed by Government.

9. The Committee regret to point out that the Government's reply is too general stating merely that the "institutions have been asked to make a review of the functioning of Nominee Directors Cell and the same would also be reviewed by Government." The Government reply is silent about the Committee's recommendation that the number of nominations should be restricted maximum to not more than eight or ten companies each and also for strengthening the Nominee Directors Cell. The Committee need hardly stress that replies to their recommendations/observations should be complete and expressed in unambiguous terms. The Committee will await necessary clarifications from the Ministry in this regard. . . .

C. Suggestions for improving functioning of Nominee Directors

Recommendation S. No. 20, Paragraph 2.20

10. The financial institutions had given certain suggestions to the Committee for improving the functioning of nominee directors. These suggestions *inter-alia* included prescribing minimum period notice for board meetings, sending agenda papers in advance, increased periodicity of Board meetings, submission of quarterly working results, compulsory formation of audit sub-committees and legal protection to nominee directors from prosecution for matters connected with assisted companies. The Committee found merit in these suggestions and desired that Ministry should examine in details the pros and cons of each of the suggestions in consultation with financial institutions for taking appropriate action. The Committee also desired to be informed of the action taken in the matter within next six months.

11. In their reply the Government have stated that matter is under examination in Government in consultation with the concerned.

12. The Committee regret to note that the Government have not been able to examine the matter within six months as desired by the Committee. The Committee take an exception to the casual manner the recommendation of the Committee has been dealt with. The Committee, therefore, urge that since the suggestions are aimed at strengthening the institution of nominee directors, the Government should complete all exercise in this regard at the earliest and take appropriate action in pursuance thereof. The Committee would like to be apprised of the Government decision on all the suggestions within three months of the presentation of the Report.

CHAPTER II

RECOMMENDATIONS THAT HAVE BEEN ACCEPTED BY GOVERNMENT

Recommendation Serial No. 1 (Paragraph 21)

Financial Institutions, having sizeable stake in the industrial concerns have been appointing their nominees on the Boards of assisted companies who *inter alia* serve as a useful tool for effective project monitoring and follow up. The nominee directors on the Boards of the assisted companies are intended not only to safeguard the interests of the institutions investing money in them, but also to serve the interests of sound public policy. The right of financial institutions to nominate such directors flows from the contractual obligation entered into between the assisted companies and institutions as also the relevant provisions in the statutes of the latter. Although the financial institutions were appointing even prior to 1971 their nominees on the boards of some of the assisted companies, the system got institutionalised with the issue of Government's guidelines on the subject in June, 1971. These guidelines were revised and amplified first in 1981 and again in 1984. The guidelines presently in operation stipulate that the financial institutions should nominate their representatives on the Boards of all assisted companies where substantial financial assistance has been sanctioned and where the convertibility clause has been incorporated in the financial assistance agreement. In other cases, the financial institutions have been given the discretion to appoint or not to appoint nominee directors on the Boards of the assisted companies. The Committee's review of the system of appointment of nominee directors, the way in which they have been functioning and the success achieved in achieving the objectives for which nominee directors are appointed, has revealed several deficiencies and weak points which need to be remedied. The Committee's findings and their recommendations for making the system really effective are set out below.

Reply of the Government

General observations of the Committee leading to their recommendations noted.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/9/87-IF.II dated 30-11-1987]

Recommendation Serial No. 2 (Paragraph No. 2.2)

As per guidelines issued by Government of India, the financial institutions are expected to appoint their nominees on the Boards of all assisted MRTP Companies. In respect of non-MRTP companies, the nominee directors are to be appointed on selective basis. The Committee are concerned to find that as on 31st March, 1986, out of 1300 assisted companies, nominee directors have been appointed by the institutions only on 1070 companies. A further break-up of these figures reveals that out of 324 assisted MRTP companies, nominee directors have not been appointed in 36 companies even though 12 of these companies are incurring losses. Similarly, in 194 out of 976 non-MRTP Companies nominee directors have not been appointed although 81 such companies are incurring losses. The Committee do not find any valid reason for not appointing nominee directors on such a large number of losing companies which could certainly jeopardise the security of the advances made. Unless the Financial Institutions get timely authentic reports from their nominees on the companies, it may be too late when the ultimate result is brought to notice as a fate accomplished. The Committee, therefore, desire that nominee directors should invariably be appointed in all MRTP companies and in the case of non-MRTP companies, no Board of any Company incurring losses or otherwise running into problems should be without representation from the financial institutions.

Reply of the Government

As on 31-3-1986, out of 1300 companies assisted by all institutions, they had appointed their nominees on the Boards of 1070 companies (82.3 per cent). Nominees had been withdrawn in respect of remaining 230 companies for following reasons viz.

	<i>No. of Companies</i>
Loans fully repaid	2
Loan assistance cancelled	2
Loans recalled	48
Companies taken over by Govt./Companies merged	23
Companies with very small outstanding assistance	74
Companies under liquidation	13
Companies closed	6
Others	*22
	230

*Nominees since appointed on 12 Cos. and proposal for nomination under consideration on the remaining Cos.

Institutions will review the position with reference to the latest list of assisted companies and appointed nominees where necessary, keeping these parametres in view.

(i) As on March 31, 1986, out of 324 MRTP companies assisted by institutions, they had appointed their nominees on 288 companies (89 per cent) and nominees had been withdrawn in the remaining 36 cases due to repayment of loans/merger of unit with another company/recall of loan/pending of winding up proceedings etc.

Institutions will review the position with reference to the latest list of MRTP companies and take action to appoint their nominee/s where necessary. Guidelines indicated will be kept in view.

(ii) As on March 31, 1986 there were 194 non-MRTP sick units assisted by all institutions as per GIFR definition. Institutions had appointed nominees on Boards of 149 companies (77 per cent).

Institutional nominees have not been appointed or have been withdrawn in respect of 45 companies for the following reasons viz. loans have been recalled/suits filed/proposed to be filed/companies under liquidation or management has been taken over.

Institutions will review the position with reference to the latest list of MRTP companies and take action to appoint their nominee/s on non-MRTP companies where necessary. Guidelines indicated will be kept in view.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF. II dated 30-11-1987]

Comments of the Committee

Please see Para 6 of chapter I of the Report.

Recommendation Serial No. 3 (Paragraph No. 23)

Another interesting fact which this study has brought to the fore is that Financial Institutions are normally appointing one or two nominee directors only even in cases where their share holding is large, say 51 per cent and above and have virtually left the management of such companies in the hands of private promoters. The reality is that representation of financial institutions on the boards of the assisted companies bears no relationship to the total holding of the financial institutions in the form of share capital or investments in the form of term loans. Therefore, except for the institutional nominees the boards of almost all the companies are composed entirely of promoters and their nominees irrespective of the extent of the share holding of the promoter group. The in-equity in the present arrangement whereby the interests of institutional

and other share holders remain un-represented or inadequately represented on the boards is so glaring that it needs immediate rectification. The Committee are of the firm opinion that the degree of the institutional involvement in management decision making should bear a reasonable if not exactly proportional relationship with their share-holding and investment in a company. This is all the more so as the agreement with the company or the share holding clearly vests this right in the financial institutions making the investment. The Committee recommend that financial institutions should exercise their rights as share-holder or investor of funds to appoint nominee directors in assisted companies in proportion to their share-holding and/or in terms of loans agreements. As agreed to by the Finance Secretary, full quota of Directors in cases where any financial institution singly or in conjunction with any other financial institutions is having more than 51 per cent shares but had not nominated proportionate number of directors, should be filled up forthwith. Similarly in companies where the institutional holdings is less than 50 per cent the representation may be in proportion to the total holdings and wherever the actual number of nominees is less than the entitled quota, the deficiency should be made up quickly.

Reply of the Government

The institutions have been requested that in cases of companies where Govt./institutions hold a majority share-holding, investment institutions should have adequate number of representatives as per entitlement on the Boards of assisted concerns to safeguard the interest of Govt./institutions. Development Banking Institutions should also ensure suitable representation to protect theirs and company's interests. The institutions have been requested by Government to take action and appoint nominee directors on the above lines on the basis of the shareholding by Development/Investment Institutions. We have been informed by IDBI that they would review the position and take suitable action for appointment/induction of Directors in the case of assisted companies where institutions together hold 50 per cent or more of the shareholdings. We have been informed that institutions would appoint institutional nominee directors and suitable independent outside professionals with their approval to generally ensure that such directors together form majority on the Board.

As regards companies where the institutional share-holdings was less than 50 per cent, the general consensus of the institutions is that while it is desirable to have adequate representation on three

Boards of assisted companies, the appointment of nominee directors need not necessarily be in proportion to the shareholding of the institutions in general for the following reasons:—

(a) The institutional nominee directors normally endeavour to ensure that decisions on important issues at the Board meetings are taken by consensus and thus there is hardly any voting in the Board meetings. Moreover, in view of the large stake of the financial institutions in the assisted companies by way of term loans and/or shareholding, the views of the institutional nominees, irrespective of their number, are normally given due weightage at the Board meetings. In exceptional cases where the decisions are not in the larger interest of the company, the situation can be corrected by the institutions on receipt of feedback reports from their nominees to that effect, through recourse to loan covenants.

(b) The financial institutions examine the composition of the Board before sanctioning assistance and in cases where considered necessary, suitable conditions are stipulated for broad-basing their Boards with the prior approval of the institutions. This is incorporated in the Loan Agreements as a condition and the institutions ensure that the Boards are every balanced with independent directors including the institutional nominees forming a majority. In case of joint sector companies, apart from 2 or 3 nominees of financial institutions and independent outside directors, the State level Development Financing Institutions viz. SIDCs also have their nominees on the Boards of such companies. Chairman in joint sector companies is normally nominated by the concerned SIDC.

(c) In some of the cases, investment institutions have come to acquire large shareholding by way of market purchases. This is purely in the nature of investment and in such cases, their nominees can be elected only at the General Body meetings. But such nominees will not be entitled for protection available to other institutional nominee directors.

(d) The financial institutions generally aim at professionalisation of management to encourage healthy growth of assisted companies. Appointment of nominee directors in proportion to their shareholding will give an impression that the financial institutions are running the units. And, thus in case of deterioration in working results, the functional directors/promoter Group will tend to absolve themselves of the responsibility and pass it on to the institutional nominees. Moreover, it is desirable that Boards also have adequate representation of independent outside experts with wider business

experience and perspective as also the people with expertise in specialised subjects like taxation, law, marketing, technology etc. It may not always be possible to meet all these requirements through institutional nominees alone.

As mentioned in paragraphs 1.14 and 1.21, the general consensus of the institutions is that while the appointment of nominee directors need not necessarily be in proportion to their shareholding in general, they should have adequate representation on the Boards of assisted companies where the institutions together hold 50 per cent or more of the shareholdings. This will be achieved partly by appointment of institutional nominee directors and partly through induction of suitable independent outside professionals with the approval of institutions. It would be generally ensured that such directors together form majority on the Board.

IDBI and other institutions will soon review the position and take suitable action for appointment/induction of directors accordingly.

In cases where the institutions hold less than 50 per cent shareholding, they would like to continue the existing practice of appointing 2 nominee directors (one representing development banks and the other representing investment institutions) unless circumstances warrant otherwise. However, in cases where there are dissensions in promoter family or in functional management, the representation of institutions might be adequately increased so as to ensure that the institutional nominees together with independent outside directors of their choice, form a majority on the Board.

IDBI and other institutions will soon review the position and take suitable action accordingly.

We agree with the views of the institutions. However, the institutions should keep a close watch on the performance of these units also through their nominee directors and take suitable remedial action wherever warranted.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

Recommendation Serial No. 4 (Paragraph No. 2.4)

The Committee feel that the institutional say in the management of assisted companies is more than justified on the ground that the financial institutions normally finance 80 to 90 per cent of the project cost, whereas the promoters' financial participation is only very

limited. Accordingly in cases where the share holding is more than 51 per cent, the institutions should have a greater say through loan covenants in the selection of Chairman, Managing Director, whole-time directors and other directors. Where no loan is involved (as it often happens in the case of Investment Institutions) more effective use of voting strength should be made on the basis of shareholdings.

Reply of the Government

Financial institutions by virtue of provisions in the loan agreements entered into with the assisted companies already possess the right to approve appointment/reappointment of whole-time directors. Besides, they have a right to require the companies to broaden their Board of Directors and thereby have a decisive role in the composition of Boards. Besides, the appointment/reappointment of whole-time directors is also required to be approved by the Company Law Board of Govt. of India.

The existing system is operating smoothly, and we may allow it to continue.

In cases where there are internal dissensions or other problems, we are informed that the investment institutions do exercise their voting rights on the basis of their shareholdings in consultation with financial institutions.

In all cases, where investment institutions together hold sizeable shareholding (of say more than Rs. 100 lakhs) they should invariably appoint one nominee director.

We are informed that Investment institutions will soon review the position and take suitable action.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.H. dated 30-11-1987]

Recommendation Serial No. 5 (Paragraph 2.5)

In case where the institutions have no loans outstanding but only hold shares, a convention should be built up whereby the Company should be persuaded to elect nominees of the institutions on their Boards of Directors. This in Committee's opinion would ensure proper representation of the institutions on the Boards of such companies, even after they have repaid the term loans.

Reply of the Government

Financial institutions have a right to appoint nominee even in cases where the assistance is only in the form of underwriting direct subscription to shares in terms of the provisions of the relative Agreement. In practice, they normally appoint their nominees on the Boards of such companies where such assistance is large, say Rs. 100 lakhs or so.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IP.II dated 30-11-1987]

Recommendation Serial No. 6 (Paragraph No. 2.6)

The Committee find that under the terms and conditions governing the sanction of financial assistance, the assisted units are required to broadbase their boards of directors in consultation with and to the satisfaction of the financial institutions. However, the financial institutions have not been taking requisite interest in this direction. The Committee recommend that while determining the composition of the Board of a company, the financial institutions should ensure that the board is truly broadbased, with representation from various relevant disciplines and there is no undue weightage in favour of promoters. For this it may be necessary that the composition of the Board is determined in such a manner that it comprises of not more than 1/3rd of the total number of the representatives of the promoter's group and the remaining 2/3rd consist of independent members who are professionals with expertise in finance, technical disciplines, marketing and the industry related areas etc. and the nominee directors of the institutions. In Committee's opinion that can be ensured by making suitable provisions under the covenants in the Loan Agreements entered into by the institutions with the borrower companies or, if appropriate, by making suitable provision in the Companies Act.

Reply of the Government

The financial institutions examine the composition of Boards while sanctioning assistance and where necessary stipulate a condition for broad-basing the Board. Normally, the Boards consist of representatives of promoters, functional directors, independent outside directors (having expertise in finance, technical disciplines etc.) and the institutional nominees. We are informed that it is generally ensured that the independent outside directors and the institu-

tional nominees together form a majority on the Board. Perhaps the Committee's concern would be met by the remarks indicated above.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

Recommendation Serial No. 7 (Paragraph No. 2.7)

The Committee find that the nominee directors of financial institutions are either officials of the institutions or non-officials drawn from a panel maintained for the purpose. It seems to be the common experience of all the financial institutions that in the matter of providing regular and meaningful feedback to the nominating institutions, the performance of the official nominees is much better as compared to the non-official nominee directors. The Committee, therefore, desire that there should be at least one official nominee director on each Company and non-officials should be considered for appointment only as additional nominee i.e. in addition to the official nominee of one of the institutions. This will mean that the first nominee director will always be an officer of the Institutions.

Reply of the Government

We are informed that the institutions are already following a practice whereunder atleast one of them appoints an official nominee preferably lead institution, and other appoint non-officials.

IDBI has proposed that Institutions will appoint at least one official nominee director on each company and non-officials would be considered for appointment only as additional nominee(s).

This is in accordance with the Committee's observations.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

Recommendation Serial No. 8 (Paragraph No. 2.8)

The Committee also feel that as far as possible only officials may be appointed as their nominees by the Institutions on the Boards of the assisted MRTTP Companies and in such of the non-MRTTP Companies where the stake of the institutions is very high.

Reply of the Government

IDBI has reported that Institutions will hereafter appoint atleast one official nominee on the boards of such assisted companies.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

Recommendation Serial No. 9 (Paragraph No. 2.9)

It has been brought to the Committee's notice that shortage of Officers of requisite qualification and experience was one of the reasons for not appointing more than one or two nominees on the assisted companies. This is an area which needs to be looked into. The minimum that needs to be done is that cadre of Official nominees should be suitably strengthened.

Reply of the Government

IDBI has reported that the cadre of official nominees is being strengthened by the Institutions.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

Comments of the Committee

Please see Para 6 of Chapter 1 of the Report.

Recommendation Serial No. 10 (Paragraph No. 2.10)

The Committee find that in the case of IFCI, GIC and LIC, the Chairman as also the Managing Directors of the institutions have been appointed as nominee directors in some companies. The Committee do not consider it to be a salutary practice. If the top man of a financial institution is already on the Board of Company, that could by itself be a cause for the institution not asking for any further information about the functioning of such a company from their own Chairman or Managing Director and that may weaken the vigil the financial institution has to exercise. The Committee, therefore, feel that the Chairman and Managing Directors of the institutions should not be nominated as directors on the Boards of assisted companies.

Reply of the Government

IDBI as the apex institution has reported that action has been

taken to withdraw Chairman and also Managing Directors of Institutions from the Boards of assisted companies.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

Recommendation Serial No. 11 (Paragraph No. 2.11)

The Committee have observed that although the institutions are reviewing the nominations of both officials and non-officials after a period of 3 to 4 years, in some cases nominee directors have continued for as long as 8 years on the boards of the companies. No doubt exceptions can be there in rare cases but the Committee recommend that the nominations of both officials and non-officials should be reviewed more frequently and the nominee directors should not be continued on the board of companies for very long periods as that could develop vested interests. As a guiding principle, nomination initially for a period of 3 years followed by an extension of upto 3 years should be considered desirable.

Reply of the Government

Generally, official nominees and non-official nominees are allowed to continue for a period of 4 years and 3 years respectively. However, exceptions have been made in a few cases where continuance of the institutional nominee beyond the initial term of 4 or 3 years was considered beneficial in the interest of the assisted company. We are informed by the IDBI as apex institution the extension of, upto 3 years after the initial term of 3 years will be accepted as a guiding principle.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

Recommendation Serial No. 13 (Paragraph No. 2.13)

From the information made available to the Committee, it is seen that the present panel of non-officials, consists mostly of retired officers of Government, Public Sector Undertakings, Financial Institutions and Banks. Out of 105 non-officials appointed on behalf of IDBI as many as 82 nominees are retired officials. Similarly, in GIC, there are 31 non-officials working as nominee directors out of which 28 are retired employees of GIC. Again in the case of LIC out of 42 non-officials 11 are retired officers. The Committee feel that the panel of non-officials should be enlarged with a view to include more professional like experienced engineers, Chartered Accountants, Cost

Accountants and people with experience in handling matters relating to labour. With this end in view the institutions should approach the professional bodies viz., the Institution of Chartered Accountants and the Institutions of Cost and Works Accountants to suggest the names of their members for empanelment as non-official nominees.

Reply of the Government

Institutions have a fairly diversified group of persons with qualification/experience in different disciplines and facets of industries. The panel includes professionals like Chartered Accountants, Cost Accountants, Engineers, Consultants, Solicitors etc.

We are informed that the Institute of Chartered Accountants/Cost Accountants/Company Secretaries on their own furnish names of some of their members with bio-data for empanelment.

It is true that retired officials find a larger representation on the panel but since they have long experience in various facets of industry and are also in a position to devote relatively more time to the affairs of the company where they are nominated institutions have found them useful. There is also no possibility of conflict of interest in their case.

Efforts will continue to be made by institutions to empanel a large number of professionals, experienced Chartered Accountants/Cost Accountants, Labour Experts etc. as suggested by the Committee.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF. II dated 30-11-87.]

Recommendation Serial No. 14 (Paragraph No. 2.14)

The Committee have been informed that Nominee Directors Cells have been set up by financial institutions in terms of the Government guidelines issued in March, 1984. Even though the financial institutions have maintained that these cells have been working satisfactorily, no formal review to find out their effectiveness has so far been undertaken either by the institutions or the Ministry of Finance. The Committee desire that as promised by Banking Secretary during evidence, a review should be undertaken with a view to pin-point the shortcomings in the present system and necessary remedial measures in the light of its outcome.

Reply of the Government

Government have advised the institutions that a periodic review, say six monthly, of the system of nominee directors including their performance in general should be made and brought up before the Board of the concerned institutions for their consideration.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF. II dated 30-11-87.]

Comments of the Committee

Please see para 6 of Chapter I of the Report.

Recommendation Serial No. 15 (Paragraph No. 2.15)

The Committee are convinced that financial institutions should improve the system for evaluation of the reports received from nominee directors so that more prompt and timely action could be taken on the advance signals thrown by the nominee directors based on the information which comes to their notice. The Committee also recommend that the performance of the nominee directors should be evaluated more frequently and closely and in-effective nominee directors both official and non-official should be removed/replaced without any hesitation.

Reply of the Government

Government have advised the institutions that a periodic review say 6-monthly of the system of nominee directors including their performance in general should be made and brought up before the Board of the concerned institutions for their consideration. IDBI has reported that the Nominee Directors' reports are submitted directly to the Executive Director in charge of Projects Finance and Rehabilitation Finance Depts. in case of officers in the rank of Dy. General Managers and above, and to the respective General Manager in the case of other officers. Similarly, the reports of non-officials are received at the GM's level. After the ED/GMs have gone through the reports, they are passed on to the concerned officer dealing with individual projects, for necessary follow-up action on the points mentioned therein together with specific instructions where considered necessary. All material reports are also sent to the Chairman and Managing Director through the ED. Thus, Nominee Directors' reports are first seen at the senior management level and passed on to the operational departments for follow-up action. GMs bring to the notice of Nominee Cell such cases where frequency,

adequacy or quality of feed-back, is not satisfactory. These facts are brought to the notice of concerned Nominee Directors and he is counselled suitably.

We are informed by IDBI that other institutions will also set up a formal system of review for this purpose.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF. II dated 30-11-87.]

Recommendation Serial No. 16 (Paragraph No. 2.16)

Admittedly there is need for better communication between the financial institutions and their nominee directors. The Committee, therefore, recommend that two way communication between the institutions and nominee directors, especially in case of non-officials for better appreciation and closer monitoring of the affairs of the assisted companies should be strengthened. The institutions should hold meetings of the non-official nominee directors more frequently say atleast once in a quarter for overall review of the affairs of the Company and exchange of views on the strengths and weaknesses of the project and the systems obtaining in the Company. Similarly, there should be regular exchange of views with official nominees. The institutions should also keep the nominee directors informed of all important decisions relating to the companies on the boards of which they have been nominated as nominee directors. Institutions should also insist on proper feedback from the nominee directors.

Reply of the Government

We are informed by IDBI that while official nominees have a constant dialogue with the senior dealing officers of nominating institutions, non-official nominees are also encouraged to seek advice from the nominating institutions on important matters scheduled to be discussed at Board meetings. Wherever considered necessary, institutions themselves contact them to brief on important issues.

[Ministry of Finance, Department of Economic Affairs O.M.
No. 2/3/87-IF. II dated 30-11-1987]

Recommendation Serial No. 17 (Paragraph No. 2.17)

The Committee have been informed that the nominee directors on the Board of assisted companies are intended not only to safeguard the interests of the institutions but also to serve the interests

of sound public policy. It came out during examination of financial institutions that although the role and functions of nominee directors are defined and understood clearly, yet the need for improving and streamlining the systems and procedures regarding the selection and appointment of nominee directors had been felt both by the institutions as well as the Ministry. The Committee desire that an in-depth study should be undertaken with a view to streamlining the system so as to ensure that it provides an effective monitoring and control mechanism for overseeing, the working of assisted companies and particularly the sick units.

Reply of the Government

Government have advised the institutions that a periodic review of the system of nominee directors including their performance in general should be made and brought up before the Board of Directors of the concerned institution for their consideration. Institutions have also been advised that such a review should be done 6-monthly and placed before the Board of Directors of the concerned institution.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

Comments of the Committee

Please see Para 6 of Chapter I of the Report.

Recommendation Serial No. 18 (Paragraph No. 2.18)

The Committee find that an area of great importance were the financial institutions have been lacking was that the training nominee directors. Admittedly there have been very few training programmes although the need has been felt for the same many a time. The Committee feel that since there are more than a thousand nominee directors, the institutions should give more attention to this aspect IDBI, which is working as a coordinating agency should find ways and means for having in-house training facilities in association with other financial institutions. It must ensure that necessary training is imparted to all the nominees by rotation.

Reply of the Government

IDBI has issued detailed guidelines for the use of nominee directors.

We are informed by IDBI that Institutions will hold seminars/workshops for the benefit of their nominee directors.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

Recommendation Serial No. 19 (Paragraph No. 2.19)

The Committee desire that an opportunity for the nominee directors to inter-act among themselves and exchange views which may help in cross-fertilizing experiences and improving their effectiveness may also be provided by arranging seminars and symposia for them from time to time. The role of nominee directors the aspect of their accountability and ways and means of making their functioning effective, could be reviewed and better understanding and appreciation developed through such programmes. For better interaction among nominee directors it will be worth-while to have an association of all the nominee directors which can provide a forum for more frequent inter-action.

Reply of the Government

Institutions have reported that they would be holding seminars/workshops for the benefit of their nominee directors. Detailed guidelines for the use of nominee directors have already been issued by the IDBI. It is felt that the purpose would be met equally well through the above methodology.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

CHAPTER III

**RECOMMENDATIONS WHICH THE COMMITTEE DO NOT
DESIRE TO PURSUE IN VIEW OF GOVERNMENT'S REPLIES**

NIL

CHAPTER IV .

RECOMMENDATIONS IN RESPECT OF WHICH REPLIES OF GOVERNMENT HAVE NOT BEEN ACCEPTED BY THE COMMITTEE

Recommendation Serial No. 12 (Paragraph No. 2.12)

The Committee find that financial institutions have set up Nominee Directors' Cell and the Officers attached to these cells, who function only as nominee directors, are being appointed on as many as 15 Companies each. The Committee are doubtful whether an officer will be able to do full justice if he is on the boards of 15 companies at a time. The Committee, therefore, recommend that the number of nominations should be restricted maximum to not more than eight or ten companies each and the Nominee Directors' Cell should be strengthened accordingly.

Reply of the Government

Instructions have been issued by Government to make an evaluation of the performance of these Cells to see how the constitution of the Cells in the institutions have improved the effectiveness and functioning of the nominee directors of the institutions on the Board of assisted companies. Institutions have been asked to make a review of the functioning of these Cells and the same would also be reviewed by Government.

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.F dated 30-11-1987]

Comments of the Committee

Please see Para 9 of Chapter I of the Report.

CHAPTER V

RECOMMENDATIONS IN RESPECT OF WHICH FINAL REPLIES OF GOVERNMENT ARE STILL AWAITED

Recommendation Serial No. 20 (Paragraph 2.20)

The financial institutions have given certain suggestions to the Committee for improving the functioning of nominee directors. These suggestions inter-alia include the following:—

- (i) Prescribing a minimum period of 7 days notice for Board meetings;
- (ii) Sending agenda items and background papers well in advance to the Members of the Board;
- (iii) Periodicity of Board meeting to be increased to once in 2 months instead of once in 3 months as presently obtaining;
- (iv) Submission of quarterly working results and annual capital and revenue budgets before the Board regularly and a system of presenting to the Board the half yearly audited accounts to be introduced;
- (v) Need to make it incumbent on the companies to submit to the Board periodically certain minimum management information reports covering critical areas of overall performance, key indicators for the same, financial position and operations. (The system and formats for the purpose may be evolved by the Institute of Chartered Accountants of India).
- (vi) Compulsory formation of Audit Sub-Committee;
- (vii) Legal protection to nominee directors from prosecution for matters connected with assisted companies.

Reply of the Government

Matter is under examination in Government in consultation with

the concerned. Separate report on this would be submitted to the
Committee. ..

[Ministry of Finance, Department of Economic Affairs
O.M. No. 2/3/87-IF.II dated 30-11-1987]

Comments of the Committee

Please see Para 12 of Chapter I of the Report.

NEW DELHI;
February 18, 1988

Magha 29, 1909 (S)

VAKKOM PURUSHOTHAMAN,
Chairman,
Committee in Public Undertakings.

APPENDIX I

Minutes of the 26th Sitting of Committee on Public Undertakings (1987-88) held on 20 January, 1988.

The Committee sat from 15.30 hrs. to 16.30 hrs.

PRESENT

1. Shri Jagesh Desai—*In the Chair*
2. Shrimati Prabhawati Gupta
3. Shri Damodar Pandey
4. Shri Keshorao Pardhi
5. Shri Harish Rawat
6. Shri Lal Vijay Pratap-Singh
7. Prof. Saif-ud-din Soz
8. Shri Krishna Nand Joshi
9. Shri Ram Naresh Kushawaha
10. Shri Chimanbhai Mehta
11. Shri Shanker Singh Vaghela

SECRETARIAT

1. Shri R. D. Sharma—*Chief Financial Committee Officer*
2. Shri Rup Chand—*Senior Financial Committee Officer*

* * * * *

The Committee then considered and adopted the following draft Action Taken Reports, as approved by the Action Taken Sub-Committee with minor changes as shown in Annexure II:

* * * * *

- (ii) Action Taken by Government on the recommendations contained in the Twenty-Seventh Report (1986-87) of the Committee on Public Undertakings on Nomination of Directors by Financial Institutions.

The Committee authorised the Chairman to finalise the draft Reports on the basis of factual verification by the Ministries and Undertakings concerned and present the same to Parliament.

The Committee then adjourned.

APPENDIX II

(Vide Para 3 of the Introduction)

Analysis of the Action Taken by Government on the Recommendations contained in the 27th Report of the Committee on Public Undertakings (Eighth Lok Sabha) on Nomination of Directors by Financial Institutions.

I.	Total number of recommendations	20
II.	Recommendations that have been accepted by the Government (Vide recommendation at Sl. Nos. 1-11, 13-19)	18
	Percentage to total	90%
III.	Recommendation which the Committee do not desire to pursue in view of Government's reply	Nil
	Percentage to total	Nil
IV.	Recommendations in respect of which reply of Government has not been accepted by the Committee (Vide recommendations at Sl. No. 12)	1
	Percentage to total	5%
V.	Recommendations in respect of which final replies of Government is still awaited (Vide recommendations at Sl. No. 20)	1
	Percentage to total	5%

ANNEXURE II

Changes made by the Committee in the Draft Chapter I of Action Taken Report on the recommendations contained in the Twenty Seventh Report (1986-87) on Nomination of Directors by Financial Institutions

On page 2, para 6, lines 6 and 7 *instead* of the words "Government instructions, are implemented" *read* "the recommendations made by the Committee in regard to appointment of nominee directors should be implemented...."