Who is the boss, please?

The RBI's draft code on governance is seen as being out of kilter even though well-intentioned, reports **Raghu Mohan**

"There is an inclination to write a new law or regulation, whenever some transgression takes place. You don't amend the Indian Penal Code every time a murder is committed," says M Damodaran, chairman-Excellence Enablers. It's a reference to the Reserve Bank of India's (RBI's) discussion paper on governance in banks which has raised hackles all around.

Chief executive officers (CEOs) are not to be on the nomination and remuneration committee (NRC), audit committee (AC), and the risk management committee (RMC); it is to be made of only non-executive directors (NEDs). And promoter-CEOs and non-promoter CEOs will both have to move on after completion of 10 and 15years, respectively. The sense is that it is an attempt to clip their wings. The draft appears to have imagined the board to be more "executive". In some jurisdictions in Europe, you have a supervisory board for governance and a separate one for management of the business. "The RBI's draft appears to be somewhere mid-way," says a CEO, and adds bluntly: "Frankly, it appears to me that the central bank's supervisory apparatus has pushed everything to the board."

IMAGE: ISTOCK

SIMPLY GROUNDED

- CEOs not to be on the nomination and remuneration committee, audit committee, and the risk management committee; it is to be made of only non-executive directors
- Promoter-CEOs and non-promoter CEOs will both have to move on after completion of 10 and 15 years, respectively
- Bank boards may turn out to be more executive
- In some jurisdictions in Europe, there are separate boards for governance and business, but the RBI's draft appears to be somewhere mid-way

The draft says chief risk officers (CROs) and chief compliance officers (CCOs) shall report to the RMC where CEOs find no place. And should a bank be part of a group, then the board of the bank, through its RMC, is responsible for establishing a group-wide enterprise risk-management system. Both CROs and CCOs are to have equivalence at one level below whole-time directors and CEOs. "Other business vertical heads may aspire for a similar rank and upset the hierarchy," points out a CEO.

The ghost of supervisory failures

Have shortcomings at ICICI Bank and YES Bank unduly influenced the draft governance code? "The short answer is, yes," says Kumar Saurabh Singh, partner at Khaitan & Co. Now, having only NEDs in the NRC is in line with the LODR (Listing Obligations and Disclosure Requirements); so too, in the AC. "But having only NEDs in the RMC may need a relook. It seems the intent is to provide for checks and balances, and avoid concentration of power in decision making."

"It is not desirable to have a governance arrangement which is not based on trust and appears to be confrontational. NEDs look at governance and oversight requirements and can't take on quasi-executive roles. It would also raise issues of accountability, as executive management should always remain responsible to the stake holders who operate through the board. If NED's take on a quasi-executive role, who will be accountable if matters were to go wrong? The CEO can well say that he was not in full control", argues Vimal Bhandari, executive vice-chairman & CEO of Arka Fincap.

While it is true that a few CEOs have stayed on for long, and may appear to not have paid enough attention to succession plans, there is nothing to suggest that ICICI Bank and YES Bank were not outliers. And to that extent, former RBI governor Urjit Patel is on record that the RBI has more powers over private banks compared to state-run banks, to allow two incidents colour the draft would be unfair.

Counters Amit Tandon, founder-managing director of Institutional Investor Advisory Services (IiAS): "Just as Satyam Computer Services and Sahara India are said to have an undue influence on the Companies Act (2013), it's easy to argue that developments at YES Bank have influenced RBI's thinking while framing the draft guidelines. But this misses the woods for the trees." According to him, the draft has primarily identified the control functions to provide objective assessment, reporting and, or assurance. "I don't see this as an either-or, but a more collaborative approach among the CEO, the board and the committees. It will not be correct to say that they have clipped the CEO's wings. On the contrary, they have been put in place so that the CEO can fly higher and further."

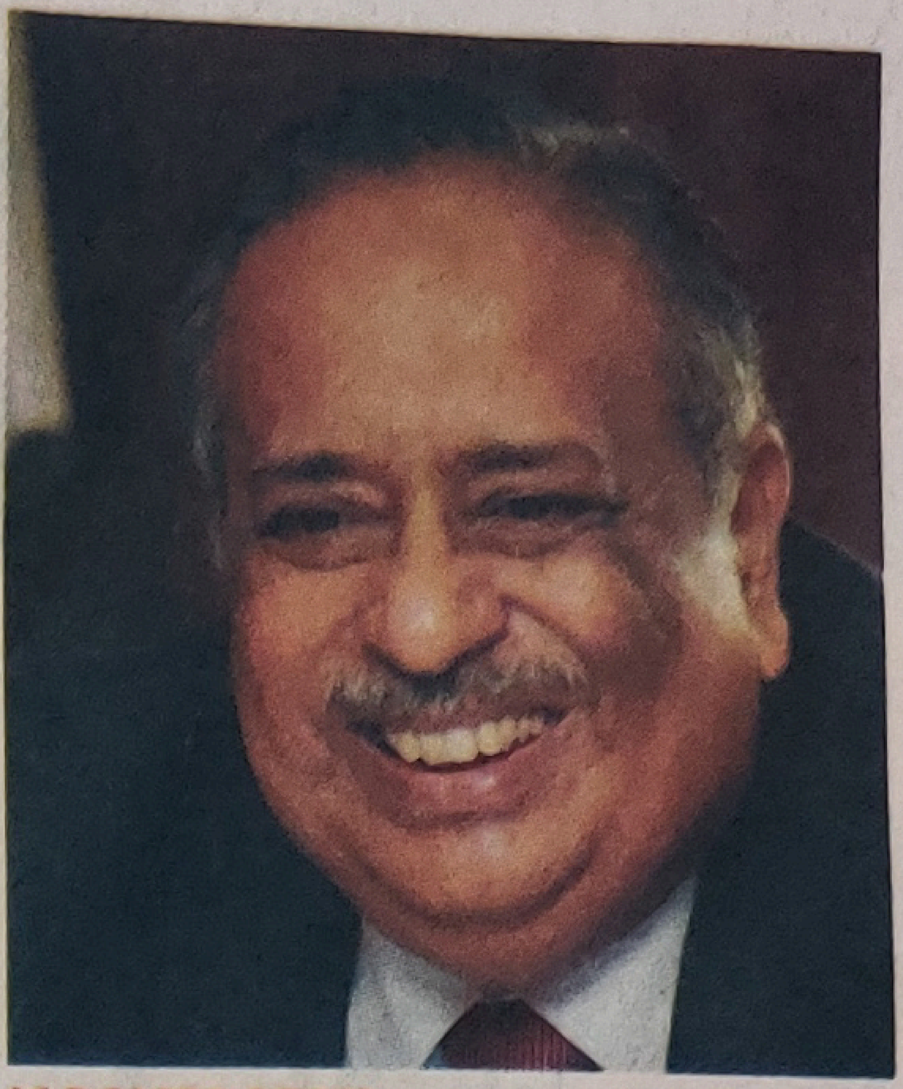
Directionally correct, but...

It pointed out that the AC has traditionally comprised only NEDs; in state-run banks, the executive director used to be a member. "The sensible compromise, which many companies are now following, is to have only NEDs on the ACB and to have the managing director, any other whole-time directors, and/or the chief financial officer as invitees to ensure that the ACB does not suffer from the absence of adequate information or insights of the management," explains Damodaran.

But he's categorical the stipulation that the CEO should not be a member of the RMC seems excessive; and appears to be premised on the apprehension that the corner-room occupant could be an adverse influence on its objectivity "As a general proposition, this does not hold water. Keeping the CEO out of the membership of the RMC is a sure recipe for disaster."

As for the tenure of CEOs, it was the central bank which settled for a maximum age of 70 years even though the P J Nayak Committee was for 65. While it is correct for the central bank to expect bank CEOs to put in place well-defined succession plans, it is misplaced of it to cap tenures. "The central question we must ask is – just for a checkbox cap of tenure, should CEOs of well-run banks be asked to vacate their positions? The regulator is shying away from using its discretionary powers and trying to find a one-size-fits-all solution to a heterogenous set of banks," said Singh.

It would not be misplaced if you were to think that the new governance code is another attempt at passing the buck.



M DAMODARAN
Chairman, Excellence Enablers

"KEEPING THE CEO OUT OF THE MEMBERSHIP OF THE RISK MANAGEMENT IS A SURE RECIPE FOR DISASTER"

AMIT TANDON
Managing director, Institutional Investor Advisory Services

"IT SEEMS THE INTENT IS TO PROVIDE FOR CHECKS AND BALANCES, AND AVOID CONCENTRATION OF POWER IN DECISION MAKING"