



## STAKEHOLDER REATIONSHIP COMMITTEE \*

### Introduction

Employees, consumers, and shareholders, as well as suppliers, special interest groups, government agencies, and the community and society as a whole all ultimately determine whether specific business actions and decisions are perceived as ethical or unethical. These groups often raise ethical issues when they exert pressure on businesses to make decisions that serve their particular agendas. Ethical issues typically arise because of conflict of interest among individuals' personal moral philosophies and values, the values and culture of the organizations in which they work.<sup>1</sup> In a business context, customers, investors and shareholders, employees, suppliers, government agencies, communities, and many others who have a "stake" or claim in some aspect of a company's products, operations, markets, industry, and outcomes are known as stakeholders. These groups are influenced by business, but they also have the ability to affect businesses.

Stakeholders provide resources that are more or less critical to a firm's long-term success. These resources may be both tangible and intangible.<sup>2</sup> Shareholders, for example, supply capital; suppliers offer material resources or intangible knowledge; employees and managers grant expertise, leadership, and commitment; customers generate revenue and provide infrastructure; and the media transmits positive corporate images.

The stakeholder concept has been reflected in the laws governing the corporates for a long period.<sup>3</sup> The labour laws seeks to ensure fair and equitable treatment to employees, the environment protection laws seeks ensure adoption of measures which will minimize the

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<sup>1</sup>Business Stakeholders, Boundless.com, available at

<https://www.boundless.com/accounting/textbooks/boundless-accounting-textbook/introduction-to-accounting-1/overview-of-key-elements-of-the-business-19/business-stakeholders-internal-and-external-117-6595/> , last assessed on 30/4/17

<sup>2</sup> Stakeholder, Investopedia, available at <http://www.investopedia.com/terms/s/stakeholder.asp>, last assessed on 30/4/17

<sup>3</sup>What are stakeholders' roles in a company, Chron, available at: <http://smallbusiness.chron.com/stakeholders-roles-company-25029.html>, last assessed on 30/4/17

negative impact on environment. Tax laws give incentives in the form of tax holidays for development of backward areas. Tax benefits in the form of exemptions for donations made to recognized funds and organizations etc.

## **TYPES OF STAKEHOLDERS**

Primary stakeholders are those whose continued association is absolutely necessary for a firm's survival; these include employees, customers, investors, and shareholders, as well as the governments and communities that provide necessary infrastructure.<sup>4</sup>

Secondary stakeholders do not typically engage in transactions with a company and thus are not essential for its survival; these include the media, trade associations, and special interest groups.<sup>5</sup>

Both primary and secondary stakeholders embrace specific values and standards that dictate what constitutes acceptable or unacceptable corporate behaviors. While primary groups may present more day-to-day concerns, secondary groups cannot be ignored or given less consideration in the ethical decision-making process.

### **Formation of Stakeholders' Relationship Committee**

Provisions for the stakeholder relationship Committee have now been introduced under Section 178 (5) of the Companies Act, 2013 ("Act"). This was not present in the erstwhile Companies Act, 1956. Before its inclusion in the Act, Clause 49 of the Listing Agreement ("Listing Agreement") required the formation of a stakeholder relationship committee for listed companies. Clause 49 of the Listing Agreement was formulated for the improvement of corporate governance in all listed companies.

Under Clause 49 of the Listing Agreement,<sup>6</sup> a committee under the chairmanship of a non-executive director and such other members as may be decided by the board of the company would be formed to specifically address the redressal of the grievances of shareholders, debenture holders, and other security holders. This committee is formed to resolve grievances

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<sup>4</sup> Identifying and analysing: stakeholders and their interests, Company tool box, available at : <http://ctb.ku.edu/en/table-of-contents/participation/encouraging-involvement/identify-stakeholders/main>, last assessed on 30/4/17

<sup>5</sup> Primary and Secondary Stakeholders of Organization, Comindwork, available at: <http://www.comindwork.com/weekly/2017-01-30/productivity/primary-and-secondary-stakeholders-of-organization>, last assessed on 30/4/17

<sup>6</sup> *Corporate Governance in listed entities - Amendments to Clauses 35B and 49 of the Equity Listing Agreement*, SEBI circular CIR/CFD/POLICY CELL/2/2014 dated 14<sup>th</sup> April 2014, Available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1397734478112.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1397734478112.pdf), last assessed on 30/4/17

of the security holders of the company including complaints related to the transfer of shares, non-receipt of balance sheet, non- receipt of declared dividends, etc.

One of the main focuses of the Act is to strengthen corporate governance by introducing strict provisions to maintain the internal management of the company. The Act by the inclusion of a separate committee to specifically address the grievances of the stakeholders provides not only a podium for them to voice their concerns but also the freedom and power to correct processes that affect the company. Measures of this sort help to improve the management and affairs of the company.

Section 178 (5) of the Act provides for the formation of a stakeholder relationship committee. This is a board committee or committee formed at the board level of a company. The board of directors of a company which consists of more than one thousand shareholders, debenture holders, deposit holders and any other security holders is to constitute a stakeholders relationship committee. The Act has allowed the inclusion of any security holders to qualify for the number of one thousand security holders along with shareholders, debenture holders, and deposit holders. Debentures have been defined<sup>7</sup> to include debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not. Deposits have been defined to include any receipt of money by way of deposit or loan or in any other form by a company but does not include such categories of the amount as may be prescribed in consultation with the Reserve Bank of India. The intention is to allow a company (be it public or private) to be able to constitute a stakeholder relationship committee for better governance and management.

The qualification of one thousand such shareholders, debenture holders, deposit holders and any other security holders may be considered at any time during a financial year. This requirement also makes it more flexible for a company to manage its number of members to be eligible to constitute a stakeholders relationship committee.

### **Composition of the Stakeholder Relationship Committee**

Such a stakeholders' relationship Committee shall consist of a chairperson who shall be a non-executive director and shall have any other members as may be decided by the Board. A non-executive director is one who is not involved in the day to day management and operations of the company and does not form part of the executive decisions of the company. Investors in a company usually prefer to be appointed as non-executive directors so they need not bear the

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<sup>7</sup> Section 2 (30), Companies Act, 2013.

liabilities of the acts or omissions carried out by the company and its founder directors. Apart from the chairperson, the board has the discretion to decide any number and qualification of members of this committee. Although the discretion of the board is a good way to permit the formation of the committee, it should always be in the best interests of the company. There should not be a member of this committee who may be an interested party to a dispute or non-compliance that has occurred in the company and referred to the stakeholder relationship committee. The board should have a policy in place to decide the members of the committee to serve the best interests of the company.<sup>8</sup> Investors who provide financial assistance to a company also usually include the appointment of their representatives on board committees such as stakeholder relationship committee, audit committee, etc. in the same form and manner as their representation on the board of the company. Such investor directors (usually of a non-executive nature) should have sufficient knowledge of the operations or the management of the company to be able to contribute productively to such committees. The board representatives may also have a casting vote in their favor in the event of a dispute that occurs in decisions or resolutions by such committee.<sup>9</sup>

The chairperson appointed in the stakeholders' relationship Committee or any other member of the company, (due to reasons of his absence, provided the chairperson authorizes him) is mandatorily required to attend the general meetings of the company<sup>10</sup>.

### **Functions of Stakeholder Relationship Committee**

The main function of the stakeholders' relationship Committee is to consider and resolve the grievances of the security holders of the company. Although this is a very wide function of the committee, the Act does not provide for enabling of provisions as to how this would be implemented. Will the company have a policy in place to implement the means and methods of resolving a dispute? Or will they take it on a case-to-case basis and consider the best method to resolve a grievance? The manner of resolution and situations of a deadlock are also things that need to be considered by the board for the policies in such committees. There seems to be no clarity on this front, and while some direction is always good to ensure practices are created and followed, complete discretion may allow each company to customize it according to their businesses and management.

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<sup>8</sup> *BOARD COMMITTEES : A HAND BOOK The Companies Act, 2013*, ICSI, Series, available at: <https://www.icsi.edu/WebModules/CompaniesAct2013/Board%20Committees.pdf> , last assessed on 30/4/17

<sup>9</sup> *Board Committees: Stakeholder relationship committee*, AishMGharana Law Governance and Responsibility, available at: <https://aishmgharana.me/tag/stakeholders-relationship-committee/> , last assessed on 30/4/17

<sup>10</sup> Section 178 (7), Companies Act, 2013.

The Act also does not provide for any specific kind of grievances that may be considered by the stakeholder relationship committee and while this may have both its pros and cons, the onus is on the board to decide the priority for a particular grievance of a stakeholder. Some examples may be non-receipt of dividends or financial statements. The recourse for these grievances are already available in law, but the creation of a stakeholder relationship committee helps to resolve such grievances at an earlier and less disputed level. Shareholders may approach the committee or submit their grievance, and if it is something that is procedural, it could be managed by the company itself and if it is something that needs the inputs of a professional, board may decide to engage the services of such professional to resolve the grievance. The biggest advantage of such a stakeholder relationship Committee is the non-adversarial approach that would be adopted by the company to resolve issues and to ensure smooth management of the company.<sup>11</sup>

The Act also does not provide for the time periods within which a particular grievance needs to be resolved. This may work against the interest of the company as there is no statutory requirement binding the company to resolve the matter. The board should, in the best interests of the company, provide for timelines based on the grievance submitted to the board or the board may also categorize the issues by priority, provided it is done in the best interests of the company.

### **Penalties**

The Act further provides for penalty<sup>12</sup> for non-compliance with provision 178, i.e., constitution and functioning of a stakeholder relationship committee in a company which consists of more than one thousand shareholders, debenture holders, deposit holders and any other security holders.

Such company shall be punishable with fine which shall not be less than Indian Rupees one lakh but which may extend to Indian Rupees five lakh and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than Indian Rupees twenty-five thousand but which may extend to Indian Rupees One lakh or with both. The Act has made stringent provisions for non-compliances leading to not just fine but also including imprisonment to every officer in default in the company. The only exception to the contravention of Section 178 is in situations where

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<sup>11</sup> *An Overview On Stakeholder Relationship Committee*, Poonam Sharma, [blog.ipleaders.in](http://blog.ipleaders.in), available at: <https://blog.ipleaders.in/overview-stakeholder-relationship-committee/>, last assessed on 30/4/17

<sup>12</sup> Section 178 (8), Companies Act, 2013.

the non-consideration of a resolution of any grievance by the Stakeholder Relationship Committee is in good faith. It is suggested that there should be reasoned responses to the non-consideration of any grievance or the non-consideration of a resolution of any grievance (provided it is in good faith) submitted by a stakeholder or debenture holder or deposit holder or any other holders by the committee.

The Act has made stringent provisions for non-compliances leading to not just fine but also including imprisonment to every officer in default in the company. The only exception to the contravention of Section 178 is in situations where the non-consideration of a resolution of any grievance by the Stakeholder Relationship Committee is in good faith. It is suggested that there should be reasoned responses to the non-consideration of any grievance or the non-consideration of a resolution of any grievance (provided it is in good faith) submitted by a stakeholder or debenture holder or deposit holder or any other holders by the committee.

## **Conclusion**

Stakeholder engagement is an alliance-building tool. Corporations practice stakeholder engagement in an effort to understand the needs of their stakeholders, create partnerships and promote dialogue. Stakeholder engagement identifies stakeholders, assesses stakeholder needs, develops stakeholder relations plans and forms alliances with stakeholders.<sup>13</sup>

Stakeholder engagement leads to increased transparency, responsiveness, compliance, organizational learning, quality management, accountability and sustainability. Stakeholder engagement is a central feature of sustainability performance.

Stakeholder engagement is undertaken for numerous reasons which include:

- Improved corporate responsibility and financial performance across the globe.
- To avoid conflict through negotiation, mediation and collaborative learning.
- Development of a shared vision to direct future business decisions and operations.
- To innovate through stakeholder collaboration.

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<sup>13</sup> *GOVERNANCE, BUSINESS ETHICS AND SUSTAINABILITY*, ICSI, available at: <http://www.icsi.in/Study%20Material%20Professional/GBES.pdf>, last assessed on 30/4/17

Agreement”) required the formation of a stakeholder relationship committee for listed companies. Clause 49 of the Listing Agreement was formulated for the improvement of corporate governance in all listed companies.

Stakeholder engagement involves following steps:

1. Identify stakeholder
2. Establish the goals and objectives of the company for stakeholder engagement.
3. Identify stakeholder needs and interests.
4. Determine the stakeholder engagement strategy.
5. Evaluate outcome and internalize learnings.

Corporations are often confronted with the difficulty of balancing competing or opposing stakeholder needs or demands. The success of stakeholder engagement is initially dependent upon the quality of stakeholder analysis.

While stakeholders can be hopeful that more processes being included in a company will only improve the management and operations of a company, it is still to be seen how the inclusion of such a committee would improve the corporate governance of a company. It is a suggestion that specific guidelines be provided for situations where the company is unable to resolve a grievance of a stakeholder, and this may be referred to a higher committee (possibly within the company) for guidance. It is also suggested that a report be included by this committee which records the manner and methods of resolution of grievances in every financial year in the company. This may also be included in the board report of the company to act as a precedent for the company.

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