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# Options for nominees: case could set precedent

The state-owned insurance firms claim that guidelines issued by Sebi prohibit nominee directors from participating in any stock option programme

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A case before the Bombay high court could decide on whether nominee directors on the boards of companies are eligible for stock option schemes.

Last week, the court stopped two nominee directors on the board of engineering firm Larsen & Toubro Ltd (L&T) from exercising their stock options until a case related to the same is heard on 12 June. Nominee directors are people who represent a large institutional shareholder on the board of a company. In L&T's case, Kranti Sinha represents Life Insurance Corporation of India (LIC) and B.G. Deshmukh, General Insurance Corporation of India (GIC).

The two state-owned insurance firms claim that guidelines on employee stock options issued by stock market regulator Sebi prohibit nominee directors from participating in any stock option programme. The problem is that Sebi's guidelines are silent on the issue of stock options and nominee directors. However, they do state that "nominee directors appointed by an institution which has invested in or lent to the company shall be deemed to be independent directors." And they also allow for independent directors to be eligible for stock options.

LIC's Sinha and GIC's Deshmukh retired from their respective firms, but continued to serve as "nominee directors" at L&T. The two insurance firms claim that the 20,000 shares given to Sinha and the 30,000 shares given to Deshmukh under the employee stock option programme are beyond the terms of their agreement with the individual directors and L&T and flout guidelines set by Sebi. Deshmukh could not be contacted and Sinha said he would not comment on the matter while it was before the court.

D.K. Mehrotra, managing director, LIC, said neither his company nor Sinha were eligible for stock options. "The nominee director is on the board of the company because of LIC," he added. "He is supposed to project the interest of the financial institution and not accept ESOPs." L&T's representatives refused to comment and GIC representatives could not be reached.

With no clear guidelines from Sebi on nominee directors, lawyers are looking at the regulator's rules regarding stock options for independent directors and promoters or directors with a stake in the company. The lawyers said they were still not clear

if nominee directors are independent directors for the purpose of participating in stock option programmes.

The case is rendered even more complex by the fact that Sebi's guidelines state that "... a director, who either by himself or through his relative or through any body corporate, directly or indirectly holds more than 10% of the outstanding equity shares of the company, shall not be eligible to participate." According to data available on BSE website, LIC owns a 15.97% stake in L&T. GIC has 2.66%.

"Any guidelines that come must be looked at for their fundamental purpose and intention." said Nitin Potdar, partner at law firm J. Sagar Associates and attorney for LIC and GIC. "And the basic purpose here clearly is to compensate and incentivize employees of the company. And, therefore, whenever shares are given one has to see if he is serving the company in that sense."

Also, the insurance companies said the appointment contract between the nominee directors and L&T prohibited additional compensation beyond travelling and meeting fees. Nishith Desai of law firm Nishith Desai Associates said it is usual for nominee directors to return the compensation they get other than the fee for each meeting. However, a partner at another law firm, who spoke on condition of anonymity, said Singh and Deshmukh were no longer officers of the insurance firms and that much would depend on the contract between the insurance firm and its nominee on the board of the company. Ravi Kadam, advocate general of Maharashtra, appeared on behalf of LIC before the court and senior counsel J.J. Bhat for GIC, under the instruction of Nitin Potdar.

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