



APAC NEWSLETTER
Legal, Compliance and ESG

06 May 2022

Dear Readers,

We bring to your reading and attention following topics:

- A. *Guidelines on Compensation of Key Managerial Personnel (KMP) and Senior Management in NBFCs*----- 2**
- B. *NOTARY AND IT'S FUNCTIONS EXPLAINED*----- 4**
- C. *CHALLENGES FOR ARBITRATION IN INDIA* ----- 6**

A. Guidelines on Compensation of Key Managerial Personnel (KMP) and Senior Management in NBFCs

Reserve Bank of India (“RBI”) has released a circular dated April 29, 2022 (“Circular”) on “Guidelines on Compensation of Key Managerial Personnel (KMP) and Senior Management in NBFCs”.

RBI vide circular dated October 22, 2021 issued a revised Scale Based Regulatory (SBR) framework for NBFCs. In terms of that circular, in order to address issues arising out of excessive risk taking caused by misaligned compensation packages, NBFCs were required to put in place a Board approved compensation policy which shall at minimum include, (a) constitution of a Remuneration Committee, (b) principles for fixed/ variable pay structures, and (c) malus/ clawback provisions. Further, it was decided that the Board of NBFCs shall delineate the role of various committees, including Nomination and Remuneration Committee (NRC).

The guidelines are intended only for providing broad guidance to NBFCs and their NRCs in formulating their compensation policy. While formulating the compensation policy, it has to be ensured that all statutory mandates and the rules and directions issued under them are fully complied with. These guidelines will be applicable for fixing the compensation policy of Key Managerial Personnel and members of senior management of all Non-Banking Financial Companies under SBR framework, except those categorised under ‘Base Layer’3 and Government owned NBFCs.

RBI has now decided to release detailed guidelines in this regard as follows:

1. Nomination and Renumeration Committee (NRC)

The Boards of all applicable NBFCs shall constitute a Nomination and Remuneration Committee (NRC). The NRC shall have the constitution, powers, functions, and duties as laid down in section 178 of the Companies Act, 2013. The NRC, *inter alia*, shall also have the mandate to oversee the framing, review, and implementation of compensation policy of the company which should have the approval of the board. The NRC may work in close coordination with Risk Management Committee (RMC) of the company to achieve effective alignment between compensation and risks. Further, the NRC may ensure that compensation levels are supported by the need to retain earnings of the company and the need to maintain adequate capital based on Internal Capital Adequacy Assessment Process (ICAAP). NRC may also ensure ‘fit and proper’ status of proposed/existing directors and that there is no conflict of interest in appointment of directors on Board of the company, KMPs and senior management.

2. Principles for compensation

- a. Components and risk alignment: The compensation of Key Managerial Personnel (KMPs) and senior management needs to be reasonable, recognizing all relevant factors including adherence to statutory requirements and industry practices and may comprise of fixed and variable pay components aligned effectively with prudent risk taking to ensure that compensation is adjusted for all types of risks, the compensation outcomes are symmetric with risk outcomes, compensation pay-outs are sensitive to the time horizon of the risks, and the mix of cash, equity and other forms of compensation are consistent with risk alignment.

- b. Composition of fixed pay: All fixed items of compensation, including perquisites and contributions towards superannuation/retiral benefits, may be treated as part of fixed pay. All perquisites that are reimbursable may also be included in the fixed pay so long as there are monetary ceilings on these reimbursements. Monetary equivalent of benefits of non-monetary nature may also be part of fixed pay.
- c. Principles for variable pay:
 - aa. Composition of variable pay: The variable pay may be in the form of share-linked instruments, or a mix of cash and share-linked instruments (which shall be in conformity with relevant statutory provisions).
 - bb. Proportion: proportion of variable pay in total compensation needs to be commensurate with the role and prudent risk-taking profile of KMPs/ senior management. At higher levels of responsibility, the proportion of variable pay needs to be higher. There should be proper balance between the cash and share-linked instruments in the variable pay in case the variable pay contains share linked instruments. The variable pay should be truly and effectively variable and can be reduced to zero based on performance at an individual, business-unit, and company-wide level and in order to do so, performance measures and their relation to remuneration packages should be clearly defined at the beginning of the performance measurement period to ensure that the employees perceive the incentive mechanism.
 - cc. Deferral of variable pay: Certain portion of variable pay, as decided by the Board of the company, may be deferred to time horizon of the risks and not all variable pay may be paid immediately. The portion of deferral arrangement may be made applicable for both cash and non-cash components of the variable pay. Deferral period for such an arrangement may be decided by the Board of the company.
 - dd. Control and assurance function personnel: KMPs and senior management engaged in financial control, risk management, compliance and internal audit may be compensated in a manner that is independent of the business areas they oversee and commensurate with their key role in the company. Accordingly, such personnel may have higher proportion of fixed compensation. However, a reasonable proportion of compensation may be in the form of variable pay, so that exercising the options of malus and/or clawback, when warranted, is not rendered infructuous.
- 3. Guaranteed bonus: Guaranteed bonus may not be paid to KMPs and senior management. However, in the context of new hiring joining/sign-on bonus could be considered. Such bonus will neither be considered part of fixed pay nor of variable pay.
- 4. Malus/claw back: deferred compensation may be subject to malus/clawback arrangements in the event of subdued or negative financial performance of the company and/or the relevant line of business or employee misconduct in any year. A representative set of situations may be identified by the NBFC, which require them to invoke the malus and clawback clauses that may be applicable on entire variable pay. While setting criteria for the application of malus and clawback, NBFCs may also specify a period during which malus and/or clawback can be applied, covering at least the deferral and retention periods.

The guidelines shall come into force from April 01, 2023.

B. NOTARY AND IT'S FUNCTIONS EXPLAINED

~ Vivek Ugale, Senior Officer- Legal

Introduction:

The Notaries Act provides for the appointment of Notaries. The Central Government for the whole or any part of India or any State Government for the whole or any part of the State, may appoint as Notaries any legal practitioners or other persons who possess such qualification as may be prescribed. As per section 2(d) of the Notaries Act, 1952, "Notary" means a person appointed such as under this act.

Who can be called as Notary?

A person authorized to perform certain legal formalities, especially to draw up or certify contracts, deeds, and other documents for use in other jurisdictions.

Functions of Notary

As per Section 8 of the Notaries Act, a notary may do all or any of the following acts by virtue of his office, namely;

- i. verify, authenticate, certify or attest the execution of any instrument;
- ii. present any promissory note, hundi or bill of exchange for acceptance or payment or demand better security;
- iii. note or protest the dishonour by non-acceptance or non-payment of any promissory note, hundi or bill of exchange or protest for better security or prepare acts of honour under the Negotiable Instruments Act, 1881 (XXVI of 1881), or serve notice of such note or protest;
- iv. note and draw up ship's protest, boat's protest or protest relating to demurrage and other commercial matters;
- v. administer oath to, or take affidavit from, any person;
- vi. prepare bottomry and respondentia bonds, charter parties and other mercantile documents;
- vii. prepare, attest or authenticate any instrument intended to take effect in any country or place outside India in such form and language as may conform to the law of the place where such deed is entitled to operate;
- viii. translate, and verify the translation of, any document from, one language into another;
- ix. any other act which may be prescribed.

The above acts performed by Notaries shall be deemed to be a notarial act when it is done by a notary under his signature and official seal. Every court shall take judicial notice of the other seals of a Notary as provided in Section 57 (7) and section 85 of the Indian Evidence Act, 1872.

Stamp Duty:

Before making a notarial endorsement, it is the duty of the Notary to see that the instrument is duly stamped, if it is not, he can hold it under section 33 (1) of the Stamp Act and after he has made the Negotiable endorsement, it is further liable to a duty under section 42 of the Stamp Act if the stamp duty is underpaid.

Reciprocal Arrangements for recognition of Notarial acts done by foreign Notaries:

Section 14 of the Notaries Act specifies that if the Central Government is satisfied that by the law or practice of any country or place outside India, the notarial acts done by Notaries within India are recognised for all or any limited purposes In that country or place, the Central Government, may by notification in the official gazette, declared that the Notarial acts lawfully done by Notaries within such country or place shall be recognised within India for all purposes or, as the case may be, for such limited purposes may be specified in the notification.

C. CHALLENGES FOR ARBITRATION IN INDIA.

~ Yogesh Babar, Assistant Manager- Legal

Introduction

According to recent reports, India is estimated to have 3.53 crore pending cases in total, where 58,669 cases are pending in supreme court, 43,63,260 pending cases across all high courts and a whopping 3.11 crore pending cases only across all District and Subordinate courts in India. Despite these statistics, more and more people are tilted towards the judiciary to resolve their disputes.

Alternate dispute resolution methods are very helpful and very crucial for any business firm. It helps them to resolve any disputes internally and with a greater pace than any Judicial system can ever do. The parties involved in an Arbitration proceeding have power to add their own terms and conditions, like they would do in any other form of contract or agreement.

Many business houses opt for Alternate Dispute Resolution methods like Arbitration in their contracts and agreement for a speedy method to resolve disputes. And hence, it is clear that Arbitration has many advantages and useful applications.

Arbitration and its Process:

Arbitration is a process of resolving disputes between private entities, outside the court machinery. In simple terms, arbitration is a process when two or more parties decide to settle a dispute outside the court(s).

A simplified arbitration agreement involves following steps:

- The parties to a contract/agreement, adds arbitration clause into their agreement/contract and if and when any dispute arises between them, one party informs the other party about the dispute by issuing arbitration notice.
- This is followed by response by the other party and subsequent appointment of an arbitrator, decision on rules and procedures, place of arbitration and language.
- Once the arbitration proceedings commence, there are formal hearings and written proceedings.
- The arbitrator, if the matter so requires, issues interim reliefs followed by a final award which is binding on both parties.
- IF either of the parties, unhappy with the award, challenges it before the court. This can be before the appellate court, High Court or Supreme Court depending upon the matter.

Reasons for Hindrance in Growth of Arbitration in India

The Constitution of India provides 'one' with many reliefs and aims to deliver justice to each person, who has been wronged. One such relief is the Process of arbitration that has been provided under Arbitration and Conciliation Act, 1996 (A&C Act). But due to the following reasons, Arbitration in India has not grown properly as it is accepted to be:

- **Conventional thinking of Indians**

Although India is moving towards modernization, it is yet a developing country. Which means, most people are ignorant towards arbitration and still trust courts more than alternate dispute resolution. This is not necessarily a bad thing, putting faith in one's judicial system, but when the citizens of a country are ignorant and are unwilling towards change, this kind of orthodox thinking can really harm rather than helping anyone.

- **Lack of Proper Laws**

The Arbitration and Conciliation Act was introduced in 1996, and last amended in 2015. In India, there is a serious need for introduction of more comprehensive law regarding arbitration process and proceedings. The law makers need to extensively study the problems regarding the needs and requirements of business houses, that usually deals with arbitration proceedings. The laws must become strict and more carefully elaborated so that more and more people gain assurance in Arbitration than the Judicial System. In simple terms, most of the people are still not willing to take risks or a leap of faith regarding matters of large magnitude that they may face in a business.

- **Intervention of Courts in Arbitration Proceedings**

The intervention of courts in arbitration proceedings shall be kept to minimum. Due to such interventions, those who opt for arbitration rather than pleading to a court, also result in inclination towards courts furthermore. People sometimes find it better to approach the court at first. Court intervention should be kept in check, not only the intervention during arbitral proceedings, but the intervention after the proceedings are concluded. This means, there must be a limited scope to challenge the arbitral award under Section 34 of Arbitration Act, 1996. In *White Industries Vs. Republic of India*, two issues arise: a) Intervention of judiciary and b) Delay in arbitration. And so it was well debated and agreed that the involvement of the judiciary should be minimized to an extent.

- **Lack of Awareness**

One of the major issues due to which Arbitration is not growing in India is because of lack of awareness among the people. Some businessmen, advocates or legal advisors are only aware of the situation relating to arbitration proceedings and due to this unawareness, many small-scale businessmen or various newcomers who are not aware of such remedies are left out of the scope of such proceedings.

The above-mentioned points are the main reason as to why arbitration is not growing faster in India. And now, we must discuss how we can overcome these problems, so as to create a better image of India as a business and arbitral destination.

Addressing Issues and Overcoming them:

- **Creating Awareness**

Among the people is the first and foremost need, if we want to create a better position for arbitration in India. Messaging is critical. Promoting arbitration and, therefore, preventing private

APAC Financial Services Private Limited

First Floor, Ashford Centre, Shankar Rao Naram Marg, Lower Parel (W), Mumbai 400013

players to rush to the courts without resorting to the relevant provisions of arbitration in the contract, must be a goal. If people are unaware of their rights, they can never seek justice. Keeping this in mind, it is very essential for us to create awareness about arbitration, its needs and its importance.

- **Mandatory Arbitration**

Should be introduced. India will not have a robust domestic arbitration environment unless institutional arbitration becomes mandatory. This can only be done if arbitration agreements mention the specific institution that will conduct arbitral proceedings.

- **Minimum Court Intervention**

Minimum court intervention is required. Arbitration is an Alternate Dispute Resolution (ADR) method, which means resolving disputes by some other method than courts, and even then, Courts are allowed to intervene in arbitration proceedings, the whole concept of ADR is lost. Court intervention should be kept to minimum and in check, like there must be a limited scope to challenge the arbitral award under Section 34 of Arbitration Act, 1996.

- **Introduction of Proper Laws**

Introduction of proper laws is also a necessary requirement in such scenarios. Arbitration laws are required to be amended on a regular basis and are crucial if our goal is to improve the conditions of the arbitration in India.

Conclusion:

Indian legal system needs a way to deal with cases that are pending in the courts, and arbitration has proved itself a boon in this regard. Arbitration is not only helpful in reducing the excess burden that is put upon the Legal System but is also helpful in many more ways, like faster decision making, less costly, parties can put forward their own terms and conditions, etc. If the above-mentioned reasons are somehow overcome, and both legislature and judiciary keep a strict check on arbitration laws, growth of arbitration in India is certain.