CORPORATE GOVERNANCE IN INDIA: AN ANALYSIS

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ABSTRACT

Corporate governance is a process, relation and mechanism set up for the corporations and firms based on certain guidelines and principles by which a company is controlled and directed. The principles provided in the system ensure that the company is governed in a way that it is able to set and achieve its goals and objectives in the context of the social, regulatory and market environment, and is able to maximize profits and also benefit those whose interest is involved in it, in the long run. The division and distribution of rights and responsibilities among different participants in the corporation (such as the board of directors, managers, shareholders, creditors, auditors, regulators, and other stakeholders) and inclusion of the rules and procedures for making decisions in corporate affairs are identified with the help of Corporate Governance mechanism and guidelines. The need to make corporate governance in India transparent was felt after the high profile corporate governance failure scams like the stock market scam, the UTI scam, Ketan Parikh scam, Satyam scam, which were severely criticized by the shareholders. Thus, Corporate Governance is not just company administration but more than that and includes monitoring the actions, policies, practices, and decisions of corporations, their agents, and affected stakeholders thereby ensuring fair, efficient and transparent functioning of the corporate management system. By this paper, the authors intend to examine the concept of corporate governance in India with regard to the provisions of corporate governance under the Companies Act 2013. The paper will highlight the importance and need of corporate governance in India. We will also discuss the important case laws which contributed immensely in the emergence of corporate governance in India.

Keywords: *Corporate governance Mechanism, Companies, Firms, Companies Act 2013*

1. INTRODUCTION

Corporate governance defined as "the set of conditions that shapes the ex post bargaining over the quasi-rents generated by a firm."[1]

Corporate governance has also been more narrowly defined as "a system of law and sound approaches by which corporations are directed and controlled focusing on the internal and external corporate structures with the intention of monitoring the actions of management and directors and thereby, mitigating agency risks which may stem from the misdeeds of corporate officers."[2]

We may infer that Corporate governance is a process, relation and mechanism set up for the corporations and firms based on certain guidelines and principles by which a company is controlled and directed. The principles provided in the system ensure that the company is governed in a way that it is able to set and achieve its goals and objectives in the context of the social, regulatory and market environment, and is able to maximize profits and also benefit those whose interest is involved in it, in the long run. The division and distribution of rights and responsibilities among different participants in the corporation (such as the board of directors, managers, shareholders, creditors, auditors, regulators, and other stakeholders) and inclusion of the rules and procedures for making decisions in corporate affairs are identified with the help of Corporate Governance mechanism and guidelines.

The framework of corporate governance consists of:

(1) Express or implied contracts between the stakeholders and the company for the distribution of rights, duties, rewards and liabilities,etc among different participants in the corporation.

(2) Procedure for proper control and supervision of information flow in the company, i.e., a proper mechanism of checks-and-balances, and

(3) Procedures for resolving and reconciling the conflicting interests and decisions of different participants in the corporation.

This mechanism ensures accountability of the Board of Directors to all stakeholders of the corporation i.e. managers, shareholders, suppliers, creditors, auditors, regulators, employees, customers and society in general; for giving the company a fair, clear and efficient administration. So it is not just mere company administration but a corporate management system. It is a code of conduct that must be followed for running and proper functioning of a corporate entity.

2. CORPORATE GOVERNANCE FRAMEWORK IN INDIA

Ever since India's biggest-ever corporate fraud and governance failure unearthed at Satyam Computer Services Limited, the concerns about good Corporate Governance have increased phenomenally.

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[1] Luigi Zingales, 2008. "corporate governance," The New Palgrave Dictionary of Economics, 2nd Edition. Abstract.

[2] *Sifuna, Anazett Pacy (2012). "Disclose or Abstain: The Prohibition of Insider Trading on Trial". Journal of International Banking Law and Regulation.*

Internationally, there has been a great deal of debate going on for quite some time. The famous Cadbury Committee defined "Corporate Governance" in its Report (Financial Aspects of Corporate Governance, published in 1992) as "the system by which companies are directed and controlled".

The Organisation for Economic Cooperation and Development (OECD), which, in 1999, published its Principles of Corporate Governance gives a very comprehensive definition of corporate governance, as under:

"a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined. Good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and shareholders, and should facilitate effective monitoring, thereby encouraging firms to use recourses more efficiently."

2.1. Regulatory framework on corporate governance

The Indian statutory framework has, by and large, been in consonance with the international best practices of corporate governance. Broadly speaking, the corporate governance mechanism for companies in India is enumerated in the following enactments/ regulations/ guidelines/ listing agreement:

1. The Companies Act, 2013 inter alia contains provisions relating to board constitution, board meetings, board processes, independent directors, general meetings, audit committees, related party transactions, disclosure requirements in financial statements, etc.

2. Securities and Exchange Board of India (SEBI) Guidelines: SEBI is a regulatory authority having jurisdiction over listed companies and which issues regulations, rules and guidelines to companies to ensure protection of investors.

3. Standard Listing Agreement of Stock Exchanges: For companies whose shares are listed on the stock exchanges.

4. Accounting Standards issued by the Institute of Chartered Accountants of India (ICAI): ICAI is an autonomous body, which issues accounting standards providing guidelines for disclosures of financial information. Section 129 of the New Companies Act inter alia provides that the financial statements shall give a true and fair view of the state of affairs of the company or companies, comply with the accounting standards notified under s 133 of the New Companies Act. It is further provided that items contained in such financial statements shall be in accordance with the accounting standards.

5. Secretarial Standards issued by the Institute of Company Secretaries of India (ICSI): ICSI is an autonomous body, which issues secretarial standards in terms of the provisions of the New Companies Act. So far, the ICSI has issued Secretarial Standard on "Meetings of the Board of Directors" (SS-1) and Secretarial Standards on "General Meetings" (SS-2). These Secretarial Standards have come into force w.e.f. July 1, 2015. Section 118(10) of the New Companies Act provide that every company (other than one person company) shall observe Secretarial Standards specified as such by the ICSI with respect to general and board meetings.

3. CORPORATE GOVERNANCE UNDER THE COMPANIES ACT, 2013

Many high profile corporate governance failure scams like the stock market scam, the UTI scam, Ketan Parikh scam, Satyam scam, which was severely criticized by the shareholders, called for a need to make corporate governance in India transparent as it greatly affects the development of the country.

The Indian Companies Act of 2013 introduced some progressive and transparent processes which benefit stakeholders, directors as well as the management of companies. Investment advisory services and proxy firms provide concise information to the shareholders about these newly introduced processes and regulations, which aim to improve the corporate governance in India.

Corporate advisory services are offered by advisory firms to efficiently manage the activities of companies to ensure stability and growth of the business, maintain the reputation and reliability for customers and clients. The top management that consists of the board of directors is responsible for governance. They must have effective control over affairs of the company in the interest of the company and minority shareholders. Corporate governance ensures strict and efficient application of management practices along with legal compliance in the continually changing business scenario in India.

Corporate governance was guided by Clause 49 of the Listing Agreement before introduction of the Companies Act of 2013. As per the new provision, SEBI has also approved certain amendments in the Listing Agreement so as to improve the transparency in transactions of listed companies and giving a bigger say to minority stakeholders in influencing the decisions of management. These amendments have become effective from 1st October 2014.

3.1. A Few New Provision for Directors and Shareholders

•One or more women directors are recommended for certain classes of companies

•Every company in India must have a resident directory

•The maximum permissible directors cannot exceed 15 in a public limited company. If more directors have to be appointed, it can be done only with approval of the shareholders after passing a Special Resolution

•The Independent Directors are a newly introduced concept under the Act. A code of conduct is prescribed and so are other functions and duties

•The Independent directors must attend at least one meeting a year

•Every company must appoint an individual or firm as an auditor. The responsibility of the Audit committee has increased

•Filing and disclosures with the Registrar of Companies has increased

•Top management recognizes the rights of the shareholders and ensures strong co-operation between the company and the stakeholders

•Every company has to make accurate disclosure of financial situations, performance, material matter, ownership and governance

3.2. Additional Provisions

• Related Party Transactions – A Related Party Transaction (RPT) is the transfer of resources or facilities between a company and another specific party. The company devises policies which must be disclosed on the website and in the annual report. All these transactions must be approved by the shareholders by passing a Special Resolution as the Companies Act of 2013. Promoters of the company cannot vote on a resolution for a related party transaction.

•Changes in Clause 35B – The e-voting facility has to be provided to the shareholder for any resolution is a legal binding for the company.

•Corporate Social Responsibility – The company has the responsibility to promote social development in order to return something that is beneficial for the society.

•Whistle Blower Policy – This is a mandatory provision by SEBI which is a vigil mechanism to report the wrong or unethical conduct of any director of the company.

4. NEED FOR CORPORATE GOVERNANCE

The need for corporate governance is highlighted by the following factors:

(i) Wide Spread of Shareholders:

Today a company has a very large number of shareholders spread all over the nation and even the world; and a majority of shareholders being unorganised and having an indifferent attitude towards corporate affairs. The idea of shareholders' democracy remains confined only to the law and the Articles of Association; which requires a practical implementation through a code of conduct of corporate governance.

(ii) Changing Ownership Structure:

The pattern of corporate ownership has changed considerably, in the present-day-times; with institutional investors (foreign as well Indian) and mutual funds becoming largest shareholders in large corporate private sector. These investors have become the greatest challenge to corporate managements, forcing the latter to abide by some established code of corporate governance to build up its image in society.

(iii) Corporate Scams or Scandals:

Corporate scams (or frauds) in the recent years of the past have shaken public confidence in corporate management. The event of Harshad Mehta scandal, which is perhaps, one biggest scandal, is in the heart and mind of all, connected with corporate shareholding or otherwise being educated and socially conscious.

The need for corporate governance is, then, imperative for reviving investors' confidence in the corporate sector towards the economic development of society.

(iv) Greater Expectations of Society of the Corporate Sector:

Society of today holds greater expectations of the corporate sector in terms of reasonable price, better quality, pollution control, best utilisation of resources etc. To meet social expectations, there is a need for a code of corporate governance, for the best management of company in economic and social terms.

(v) Hostile Take-Overs:

Hostile take-overs of corporations witnessed in several countries, put a question mark on the efficiency of managements of take-over companies. This factors also points out to the need for corporate governance, in the form of an efficient code of conduct for corporate managements.

(vi) Huge Increase in Top Management Compensation:

It has been observed in both developing and developed economies that there has been a great increase in the monetary payments (compensation) packages of top level corporate executives. There is no justification for exorbitant payments to top ranking managers, out of corporate funds, which are a property of shareholders and society.

This factor necessitates corporate governance to contain the ill-practices of top managements of companies.

(vii) Globalisation:

Desire of more and more Indian companies to get listed on international stock exchanges also focuses on a need for corporate governance. In fact, corporate governance has become a buzzword in the corporate sector. There is no doubt that international capital market recognises only companies well-managed according to standard codes of corporate governance.

5. IMPORTANCE OF CORPORATE GOVERNANCE IN INDIA / CONCLUSION

A company that has good corporate governance has a much higher level of confidence amongst the shareholders associated with that company. Active and independent directors contribute towards a positive outlook of the company in the financial market, positively influencing share prices. Corporate Governance is one of the important criteria for foreign institutional investors to decide on which company to invest in. The corporate practices in India emphasize the functions of audit and finances that have legal, moral and ethical implications for the business and its impact on the shareholders. The Indian Companies Act of 2013 introduced innovative measures to appropriately balance legislative and regulatory reforms for the growth of the enterprise and to increase foreign investment, keeping in mind international practices. The rules and regulations are measures that increase the involvement of the shareholders in decision making and introduce transparency in corporate governance, which ultimately safeguards the interest of the society and shareholders. Corporate governance safeguards not only the management but the interests of the stakeholders as well and fosters the economic progress of India in the roaring economies of the world.

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