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Research Paper

Corporate Governance In India

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I. INTRODUCTION

Organizations accumulate their capital from large number of investors based in domestic and international markets. These investors expect two things, firstly safety of the money invested andsecondly a rate of return which is higher than cost of capital. Investors reflect faith in management's ability to perform and to comply with their expectations. Hence it is responsibility of the corporations' board and management to ensure that they act in their best interests at all times and adopt good governance practices to run organization.

The Companies Act 1956 provides the basic framework for regulation of all the companies. It is important for companies to adhere to values, beliefs and ethical code of conduct to run their respective businesses. A corporation should fair and transparent towards its stakeholders in all its business transactions. This is where corporate governance comes in picture. Corporate governance is about ethical conduct in business. It helps the management or the individuals to work with regard to the code of values and set of principles and choose between right and wrong among the alternative courses of action. Further, in case of conflicting interests of the parties, decisions can be based on principles influenced by the values, context and culture of the organization in line with the expectations of all stakeholders.

Corporate Governance refers to practices by which organisations are controlled, directed and governed. The fundamental concern of Corporate Governance is to ensure the conditions whereby organisation's management act in the interest of the organisation and its stakeholders and to ensure the means by which managers are held accountable to capital providers for the use of assets. To achieve the objectives of ensuring fair corporate governance, the Government of India has put in place a statutory framework.

This article highlights the concept of Corporate Governance, its need and importance in India. It also covers the pillars and key elements comprising Corporate Governance along with guiding principles governing it in India.

The Concept

Corporate Governance is a means whereby society can be sure that large corporations are well-run institutions to which investors and lenders can confidently commit their funds. It acts as a safeguard against corruption and mismanagement, while promoting fundamental values of a market economy in democratic society.It is a process set up for the firms based on certain systems and principles by which a company is governed. The guidelines provided ensure that the company is directed and controlled in a way so as to achieve the goals and objectives to add value to the company and also benefit the stakeholders in the long term.

The Organisation for Economic Cooperation and Development (OECD) 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."

Another definition which completely defines all the aspects of corporate governance is given by Shri N.R. Narayana Murthy, Chief Mentor, Infosys Limited. He has been Chairman of the Committee on Corporate Governance formed by SEBI in 2003. His definition is:

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"Corporate governance is maximizing the shareholder value in a corporation while ensuring fairness to all stakeholders, customers, employees, investors, vendors, the government and the society-at-large. Corporate governance is about transparency and raising the trust and confidence of stakeholders in the way the company is run. It is about owners and the managers operating as the trustees on behalf of every shareholder - large or small."

With the goal of promoting better corporate governance practices in India, the Ministry of Corporate Affairs, Government of India, on 1st October 2003 set up National Foundation for Corporate Governance (NFCG) in partnership with Confederation of Indian Industry (CII), Institute of Company Secretaries of India (ICSI) and Institute of Chartered Accountants of India (ICAI). In the year 2010, stakeholders in NFCG have been expanded with the inclusion of The Institute of Cost Accountants of India (ICAI) and National Stock Exchange (NSE).

Need For Corporate Governance

The last few years have seen some major scams and corporate collapse across the globe. In India, the major example is Satyam which is one of the largest IT companies in India. Ever since this biggest-ever corporate fraud and governance failure unearthed at Satyam Computer Services Limited, the concerns about good Corporate Governance have increased phenomenally. The other high profile corporate governance failure scams like the stock market scam, the UTI scam, Ketan Parikh scam, Harshad Mehta scam, were severely criticized by the shareholders. All these events have caused the public faith to shift away from free market to a more closely regulated one. This called for a need to make corporate governance in India transparent as it greatly affects the development of the country.

Transparency in corporate governance is essential for the growth, profitability and stability of any business. The need for good corporate governance has intensified due to growing competition amongst businesses in all economic sectors at the national, as well as international level.

Corporate governance is a key element in improving the economic efficiency of a firm. Good corporate governance also helps ensure that corporations take into account the interests of a wide range of constituencies, as well as of the communities within which they operate. Further, it ensures that their Boards are accountable to the shareholders. This, in turn, helps assure that corporations operate for the benefit of society as a whole. While large profits can be made taking advantage of the asymmetry between stakeholders in the short run, balancing the interests of all stakeholders alone will ensure survival and growth in the long run. This includes, for instance, taking into account societal concerns about labor and the environment.

The failure to implement good governance can have a heavy cost beyond regulatory problems. Evidence suggests that companies that do not employ meaningful governance procedures can pay a significant risk premium when competing for scarce capital in the public markets. The most common school of thought would have us believe that if management is about running businesses, governance is about ensuring that it is run properly. All companies need governing as well as managing. The aim of “Good Corporate Governance” is to enhance the long-term value of the company for its shareholders and all other partners. The enormous significance of corporate governance is clearly evident in this definition, which encompasses all stakeholders. Corporate governance integrates all the participants involved in a process, which is economic, and at the same time social. This definition is deliberately broader than the frequently heard narrower interpretation that only takes account of the corporate governance postulates aimed at shareholder interests.

To summarize, the corporate governance can help companies in the following manner:

• Better access to external finance.
• Lower costs of capital – interest rates on loans.
• Improved company performance – sustainability.
• Higher firm valuation and share performance.
• Reduced risk of corporate crisis and scandals.

Guiding Principles For Corporate Governance In India

The actual performance of the corporate governance depends on its implementation in the existing legal framework. All the parties involved in the functioning of corporate should work as per the rulebook defined by the government and other set authorities to avoid any clash of interest. The below mentioned set of guidelines will act as the roadmap and would supplement the transformation process of corporate governance.

- **Tone from the Top:**Good governance has to emerge from the tone set by top management, committed directors and executives. It is the most important factor contributing to the integrity of the process.Setting corporate culture, and the values by which executives throughout a group will behave, should be one of the board's highest priorities. The tone at the top translates and permeates into every relationship of a

corporation, including investors, employees, customers, suppliers, regulators etc. If the senior management is not personally committed to high ethical standards, no amount of board process or corporate compliance programs will serve their true purpose.

- **Balancing Act:**Corporate Governance must serve as a means to organize, structure and to establish an efficient prioritization and balancing of interests. It has two primary dimensions that need to be in balance, firstly conformity (i.e. with laws, codes, structures and roles) and secondly performance.Fair and balanced stakeholders' perspective results in long-term shareholder maximization value and maintains the company's surrounding relationships. Thus management needs to satisfy and balance the interests of a wider set of stakeholders, not simply the shareholders. Good corporate governance helps in the reconciliation of otherwise diverging interests.

- **Board composition and diversity:**Diversity of board members contributes to the success of the business. It is important in terms of thought, experience, knowledge, understanding, perspective, boosting creativity, innovation and means that a board is more capable of seeing and understanding risks and coming up with robust solutions to address them. A more diverse board of directors contributes to better performance as decisions are based on evaluating more alternatives compared to homogenous boards. They are more in touch with their customers' demands, their investors' expectations, their staff's concerns, and they have a forum in the board room where these different perspectives come together and hence, successful business strategies can be devised. If everyone on the board is on the same page, the discussions could be stagnant, decisions mundane, and the business would not get the full benefit of a rigorous debate. Diversity, in all its aspects, serves an important purpose for board effectiveness. It can widen perspectives when making decisions, avoid similarity of attitude and help companies better understand and connect with their customers and workforces.

- **Gender Diversity:**Related to the issue of board diversity is that of gender diversity in particular. Studies from various countries show that companies with a higher share of women at top levels deliver strong organizational and financial performance. It has been observed that female directors can exercise strong oversight and have a “positive, value-relevant impact” on the company. A gender-balanced board is more likely to pay attention to managing and controlling risk. According to recent estimates, women control about 70 % of global consumer spending. More women in management positions can therefore provide a broader insight in economic behaviour and consumers' choices, leading to market share gains through the creation of products and services more respondent to consumers' needs and preferences.The 2012 Women on Boards Survey finds that despite the presence of a few high profile female entrepreneurs and CEO's, India's percentage of female directors is only 5.2%, below the developing-world percentage of 7.2%, and it has not increased significantly since 2009. The Companies Bill, 2011 has taken some positive steps in this regard by providing the Central Government with the power to prescribe rules for providing minimal women's representation on corporate boards in certain classes of companies.

- **Selection process:**There is a need to adopt a more professional, independent and transparent approach to appointing independent directors. It is important for companies to align their strategic priorities to skills required in the board room and accordingly seek candidates for nonexecutive positions on the board. In order to ensure that board composition is right, it is important for the Board Chair, CEO and the rest of the board to work cohesively to identify as to what is the mix of skills that is required to take the company to the next level. Board succession planning is a process that the full board should own.

- **On-boarding/Induction process:**Independent directors on the board of a company often come from diverse backgrounds, hence a formal on-boarding program for new directors would be helpful in getting new board members up to speed quickly and enabling them to contribute sooner.It is essential to educate the independent directors on the company's business model, industry, competitive landscape, as well as its recent history of successes or problems. They should be provided a manual which gives an overview of the board's oversight processes, the company's critical financial\operational strategy and results as well as the significant financial and non-financial risks. The on-boarding program should also address the unique legal and regulatory compliance issues facing the company and its industry. Ultimately, the effectiveness of an on-boarding program would largely depend on whether the program was customized to the individual needs of a director considering his or her current expertise and role expectations.

- **Lead Independent directors:**The lead director is as an independent chief among all board members and assists in co-ordinating the activities and decisions of the other non-executive and/or independent directors,

thereby helping to ensure that board relations run smoothly and in a streamlined manner. The purpose of appointing a lead director is to foster greater transparency and accountability among senior leadership. In India, a lead director could be particularly useful as the point of contact between the promoters and the independent directors. The lead director could, help identify the critical issues for the board to deal with; assist the board in achieving consensus on significant issues; play the role of a facilitator outside the board room, especially on contentious issues; work with the CEO to prioritize issues, and enable focus on critical issues; ensure that board conversations do not veer in the direction of certain unwanted topics / individual preferences; and provide candid feedback to CEO, CFO post an executive session.

- **Information Acquisition:**The decision-making of the board is subject to the information available to them. Board members are ideally required to receive all relevant information about board resolutions and decisions, seven days before the meeting. However, practically, often documents are given immediately prior to the meeting or just a couple of days in advance. Further a vast majority of boards depend largely on management reports and informal management discussions for business information. Third party reports and stakeholder views are rarely used as tools. With such limited information, and high dependability on company sources, informed decision making is not a natural outcome. There is a need to encourage direct conversations between the independent directors, and possible one-on-one meetings between a committee of independent directors with the auditors. Independent directors need to be aware of what the right questions to ask are, what they should be particularly looking out for. Their powers, ability and responsibility should be increased. They must have right to get any data of the company and should be authorised and encouraged to take any experts opinion to help them along the decision making process.

- **Recording of Minutes:**Boards should write their minutes more explicitly. Even Right to Information, 2005 demands that the boards record their deliberations, and the process and logic of arriving at decisions. The board that minutes unanimity of views reflects what the board thought and will make for more informed board discussion avoiding hasty decisions.

- **Continuing Board Training and Education:**It is important that the people heading the organisation are upto date with the latest trends in their field and to ensure this regular training session can be conducted. Training sessions should also includehuman resources activities, which help develop soft skills. These trainings give members a chance to know each other and help in creating better understanding. This could have a verypositive impact on good governance. Most codes of best practice in corporate governancerequire directors to undergo periodic training to improve their knowledge and skills, sothey can become better leaders and change agents of their companies. Companies should be encouraged todisclose their board training and education programs.

- **Board Evaluation:**Good corporate governance warrants that the performance of the board of a company be evaluated. This would help improve effectiveness and better decision making by individual members and would help deal with strengths and weaknesses of a board. It creates a system of checks and balances and would encourage employees to perform better, thus not leaving scope for resentment amongst the employees. Further evaluations help the board to perform better as it is a systematic way of detecting the shortcomings and identifying which decisions have had the best impact. Better performance by the Board would reflect in better performance of a company.

- **Maintaining board confidentiality:**For an organization to be effective, its board, governing officers, and executive staff must conduct in order to meet the expectations of operational transparency to stakeholders and at the same time maintaining confidentiality of information in order to foster a culture for good decision making. Confidentiality is essential for an effective board process and for the protection of the corporation and its stockholders. A board should function as a collegial body, with directors respecting the confidentiality of all discussions that take place in the boardroom. A strict adherence to transparency and disclosure ensures that the board is firmly grounded in compliance with the law, while a culture of confidentiality ensures that the board has the freedom to tackle the tough issues in an apt manner.

- **Succession Planning:**A succession plan should be put in place timely. This helps as a contingency in case an emergency arises that requires a sudden transition. Steps for a successful succession should include, an action plan, a timeline, clear definition of skills required of the future leader, identification of potential successors, an objective analysis of the strengths and weaknesses of each potential successor, strengthening any areas of weakness which could be an impediment to the company in the future, integrating the best succession candidate over time, drafting the required legal documents, developing a contingency plan etc.

There can be no prescribed procedures for succession planning and selecting the CEO, and the board should fashion the principles and procedures it deems most appropriate. The existence of well-conceived and defined succession plan can go a long way in enhancing the confidence levels for all the stakeholders and can be an enormous source of reassurance.

- **Risk management:** Risk management and corporate governance principles are strongly interrelated. An organization implements strategies in order to reach its goals and each strategy has related risks that must be managed. Expertise in the area of risk management is a fundamentalrequirement for effective corporate governance and allows organizations to reach their goals.The board should, eliminate policies that promote excessive risk-taking for the sake of short term increases in stock price performance, establish compensation plans that align goals to long-term value creation, taking into consideration incentive risks, ensure that appropriate risk management systems are in place. Good governance reduces risk and facilitates its management.

- **Crisis management:**Any event that suddenly threatens a company's financial performance, reputation, employee retention, customer relations has the potential to become a full blown out crisis. An organisation response to a crisis will have a significant bearing on its short term and long-term performance.

- **Whistle Blowing:** It helps create an environment of high ethical standards, professionalism and honesty. It has been defined as the disclosure of illegal, immoral or illegitimate practices in an organisation by a current or former employee of the organisation for the benefit of the company, stakeholders and society at large. If the disclosures are found to be true suitable action should be taken and efforts should be made to protect the whistleblower.

Legal Framework For Corporate Governance In India Under The Companies Act, 2013

The Government of India has recently notified Companies Act, 2013 (“New Companies Act”), which replaces the erstwhile Companies Act, 1956. 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. TheCorporate 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.

The New Act has greater emphasis on corporate governance through the board and board processes. The New Act covers corporate governance through its following provisions:

- It introduces significant changes to the composition of the boards of directors.
- 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
- Every company is required to appoint 1 (one) resident director on its board.
- Nominee directors shall no longer be treated as independent directors.
- Listed companies and specified classes of public companies are required to appoint independent directors and women directors on their boards.
- New Companies Act for the first time codifies the duties of directors.
- Listed companies and certain other public companies shall be required to appoint at least 1 (one) woman director on its board.
- Filing and disclosures with the Registrar of Companies has increased
- Every company has to make accurate disclosure of financial situations, performance, material matter, ownership and governance

- New Companies Act mandates following committees to be constituted by the board for prescribed class of companies:
  - Audit committee
  - Nomination and remuneration committee
  - Stakeholders relationship committee
  - Corporate social responsibility committee

Pillars And Elements Of Corporate Governance

Implementation of any norm or policy is dependent on its foundation pillars. These pillars act as a guidance force that what is expected out of these policies. Similarly, key elements helps in understanding what are the constituents of the values and principles on which corporate governance of any organization is based. Hence, the pillars and key elements of corporate governance are as follows:

- **Accountability:** Itensures that management is accountable to the Board of Directors and further Board is accountable to all the concerned stakeholders.

- **Fairness**: Corporate governance plays a vital role in protecting Shareholders rights. It treats all classes of shareholders including minoritiesequally. Moreover, there has been an effective provision to redress for violations.

- **Transparency:**It ensures timely and accurate disclosure of all material matters, including the financial situation, performance, ownership and corporate governance.

- **Independence:** The procedures and structures are in place so as to minimise, or avoid completely conflicts of interest. Independent Directors and Advisers are free from the influence of others.

- **Good Board Practices:** Organizations should follow good practices like clearly defined roles and responsibilities. Directors should be very clear what is expected out of them in terms of their duties and responsibilities. There should be a well structured board with an appropriate composition and mix skill set. Director's remunerations should be in line with the best practices. Board should conduct self evaluation and management training sessions for themselves.

- **Control Environment:**Companies should follow internal control procedures which include establishment of Independent audit committee, Risk management framework, disaster recovery systems, management information systems compliance and media management.

- **Transparent Disclosure:** Apart from disclosing financial information, it is important to disclose non-financial information also. Financials should be prepared in accordance with International Financial Reporting Standards (IFRS). Company website should disclose all the relevant information which can be published to the public.

- **Shareholder Rights:**Shareholders rights should be defined very clearly. Well organised shareholder meetings should be conducted to make the former feel part of company's progress. Policy on related party transactions and other extraordinary transactions are clearly laid down. Minority shareholders are also given equal rights as their rights will be formalized. Dividend policy should be explicit and very well defined.

- **Board Commitments:** Board should create a corporate governance committee and discuss the related issues through them. This committee would develop the code of conduct, an improvement plan for the existing policies, task allocation as per the appropriate resources. It will formalize the policies and procedures and enforce them among relevant company employees.

Importance Of Corporate Governance In India

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.

II. CONCLUSION

As Indian companies compete globally for access to capitalmarkets, many are finding that the ability to benchmark against world-class organizations is essential. For a long time, India was a managed, protected economy with thecorporate sector operating in an insular fashion. But as restrictions have eased, Indian corporations are emerging on theworld stage and discovering that the old ways of doing business are nolonger sufficient in such a fast-paced global environment.

Corporate governance are the policies, procedures and rules governing the relationships between the stakeholders, directors and managers in a company, as defined by the applicable laws, the corporate charter, the company's bylaws, and formal policies.Primarily it is about managing top management, building in checks and balances to ensure that the senior executives pursue strategies that are in accordance with the corporate mission.

Since the late 1990s, significant efforts have been takenby Indian regulators, as well as by Indian industry representativesand companies, to overhaul Indian corporategovernance. Not only have reform measures been put intoplace prior to discovery of major corporate governancescandals, but both industry groups and government actorshave sprung into action following the Satyam scandal. It is essential that goodgovernance practices must be effectively implementedand enforced preferably by self-regulation and voluntaryadoption of ethical code of business conduct and ifnecessary through relevant regulatory laws and rulesframed by Government or its agencies such as SEBI,RBI, MCA etc.Thecurrent corporate governance regime in Indian straddles both voluntary and mandatory requirements. For listedcompanies, the vast majority of Clause 49 requirementsare mandatory. It remains to be seen whether some of themore recent voluntary corporate governance measures willbecome mandatory for all companies through a comprehensiverevision of the Companies Act.

The effective implementation of good governancepractices would ensure investors confidence in thecorporate companies which will lead to greaterinvestment in them ensuring their sustained growth.Thus good corporate governance would greatly benefitthe companies enabling them to thrive and prosper. Business environmentmust be maintained and operated in a manner that isconducive to investors' confidence so that both domesticand foreign investors are induced to make adequateinvestment in corporate companies. This will beconducive to rapid capital formation and sustainedgrowth of the economy. In short, the key to better corporate governance in India today lies in a more efficient andvibrant capital market.

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