Corporate Governance - The Indian Experience

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Abstract: The Companies Act lays down an elaborate structure of Corporate Governance in general, mainly because Companies are permitted to have access to the savings of public and coffers of banks by approaching for finance. All over the world, Governments have more stringent norms of Corporate Governance for those companies which are listed in the Stock Exchanges. The primary aim of listing is to enable a share of the companies to be ‘traded’ on the Stock Exchanges and also raise finance from them. When the members of public are willing to trust a company with their hard-earned savings, it is quite natural that there should be a fair play all the way. Otherwise unscrupulous businessmen are likely to resort to foul means to make a fast buck and vanish. So, in our country the Securities and Exchange Board of India, SEBI, lays down for listed companies detailed rules on the Corporate Governance. It covers the area of composition of Board of Directors, the number of times they should meet, the shareholders’ rights, the provisions for representation of small shareholders, women etc. It also lays down how much information should be disclosed to the shareholders and how quickly etc. Corporate governance will be effective and will meet the goals half way at least when the management and the professionals involved follow it in letter and spirit and NOT ONLY IN LETTER.

Keywords: Governance, Probity, Transparency, Jugaad, Compliance

I. Introduction

One has to understand what exactly is meant by the expression “Corporate Governance”.

Once there is clarity on what Governance is and what is Corporate, it is easier to appreciate the topic. The Chambers dictionary defines Governance as Government, Control, Direction, and Behavior. So, Governance can be said to mean the direction in which a thing should move. Now next comes Corporate. Corporate as everybody knows, is a form of organization that has existence independent of its owner; its powers and liabilities are separate from those of its owners. Corporate structure means how a business is organized to accomplish its objectives. Here the ownership is with shareholders and control with the Board of Directors (on behalf of the shareholders). Shareholders have shared ownership represented by shares of common stock held. Organizations are formed mostly with the aim of earning high returns for its shareholders.

In limited liability form of organization shareholders have the right to share the profits of the business, but are not personally liable for the company’s debts. Shareholders only oversee the management of the organization.

Taking these two definitions together, it can be seen that Corporate Governance is a system by which companies are directed and controlled. The key to effective corporate governance in an organization is the flow of information, right information to the right person at right time. Inaccurate information leads to ineffective follow up decisions. Decisions made should be simple and easily understood.

II. Need For The Study

Going further, one should ask why only Corporate Governance, why not partnership governance or Sole Proprietorship Governance, because partnership and sole proprietorship are also forms of business organization. Corporate Governance has gained prominence because of its relative importance as against the other forms of Organization in terms of the numbers and financials involved.

III. Review Of Literature

From the agency theory perspective, the objective of corporate governance is to ensure that managers resort to value maximizing strategies (Shleifer & Vishny, 1997). Management ownership, market for corporate control, product market competition, shareholder activism, and trading activity are considered as various mechanisms through which shareholders exercise this control (Walsh & Seward, 1990; Shleifer & Vishny, 1997). There have also been attempts to link the “resource based view” and the “managerial rents theory”

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(Castanias&Helfat, 2001) with corporate governance, in the strategic management literature. This view maintains that corporate governance is a key managerial resource or human capital, and thus a potential source of competitive advantage to the firm.

Report of the SEBI Committee on Corporate Governance (February 8, 2003) under the chairmanship of N.R. Narayana Murthy
Report of the Committee Appointed by the SEBI on Corporate Governance under the Chairmanship of Shri Kumar Mangalam Birla
Report of the SEBI Committee on Corporate Governance (October 5, 2017) under the chairmanship of Uday Kotak.

Quote from Mr. N.R. Narayana Murthy report on Corporate Governance.

In the evolution of Corporate Governance in the Country, SEBI has utilized the experience of highly respected business men to frame the guidelines and regulations. The different Committee reports of Kumar Mangalam Birla Committee, N R Narayana Murthy Committee and most recently the committee headed by Sri Uday Kotak are the basis for these regulations. SEBI has invited comments from the public on this latest report before taking action on the same.

IV. Objectives Of The Study

So, the question arises, why there should be more regulations for listed Companies. When it is looked at the role played by Stock Exchanges and the benefits enjoyed by a Listed Company, it should be able to appreciate the need for a proper Corporate Governance at least in respect of Listed Companies. Everybody knows, Public Limited Companies can access the public for raising various forms of finance as against the Private Limited Companies, which are akin to Partnerships. The lending Institutions like Banks are also more comfortable with Public Limited Companies as they are subject to greater degree of control by the Government, the Auditor and other Regulatory bodies. A Listed Company can raise equity capital from the Public at large by meeting the Regulatory requirements of SEBI.

The SEBI has laid down, for listed Companies, detailed rules on Corporate Governance. When one studies, the Corporate Governance requirements of SEBI, as laid down in the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, it is observed that these are prescriptive in nature, meaning these Regulations prescribe the minimum requirements to be complied with by a Listed Company. These cover the area of composition of Board of Directors, the number of times they should meet, the shareholders rights, the provisions for representations of small shareholders, women on the Board of Directors, etc. It also lays down clearly how much information should be disclosed to the shareholders and how quickly, etc.

They also contain some rules which restrict certain transactions or practices and also contain elaborate rules for disclosure of the factual background, so that the investing public can take a really informed decision about the issues at hand. When one understands the real import of these requirements and when one looks at the benefits that flow from out of adherence to good corporate governance practice as a matter of faith and conviction rather than complying with the letter of Law, the picture is clear.

V. Theoretical Inputs

Corporate Governance An Evaluation

Listed Companies

The expression Corporate Governance in the present context is generally understood to mean the Corporate Governance mechanism regulated by SEBI, the Securities and Exchange Board of India. The important point is Corporate Governance under these SEBI Regulations naturally covers only the Listed Companies in India. A perusal of the SEBI Regulations shows that there are exemptions even among the Listed Companies from the rigors of the Corporate Governance requirements depending upon the size of the listed entity. So, though one hears much of Corporate Governance in the newspapers and economic dailies in the Country, it covers a very minuscule fraction of the corporate structure. The listed entities in India number about 7000 though they deal with huge financial sums. A regulation over these entities will thus cover a significant portion of the economy. When one examines the prevailing Corporate Law structure in the Country, one immediately realizes that SEBI is not the only Regulator. There is a form of Corporate Governance, when one examines the Companies Act, which contains elaborate provisions of the corporate hierarchy, the restrictions in place for each organ of the structure, the elaborate powers and checks and balances in the system etc.

Corporate Governance- The Spirit Vs Letter

For a proper evaluation of the Corporate Governance system, as it operates in the Country today vis-a-vis the lofty objectives it seeks to achieve, a further appreciation of the term is necessary. First of all, one should be clear that Corporate Governance is a concept rather than a set of Rules. It also means commitment
to values, ethical business conduct and where there is no misuse of corporate funds and the structure for personal gain. Corporate Governance, though it would be seen later, in practice it got reduced to a form filling exercise, goes beyond the realm of Law. It stems from the culture and mindset of Management and can be never regulated by the Legislation alone. To quote from Mr. N.R. Narayana Murthy report on Corporate Governance, “the important point is that Corporate Governance is a concept, rather than an individual instrument. It includes debate on the appropriate management and control structures of a Company. Further it includes the rules relating to the power relations between owners, the Board of Directors, Management and, last but not least, the stakeholders such as employees, suppliers, customers and the public at large.”

Corporate Governance is beyond the realm of law. It stems from the culture and mindset of management and cannot be regulated by legislation alone. It is about openness, integrity and accountability. What legislation can and should do is to lay down a common framework – the “form” to ensure standards. The “substance” will ultimately determine the credibility and integrity of the process. Substance is inexorably linked to the mindset and ethical standards of management. By integrity is meant the total transparency of the management in its dealing with Employees, Suppliers, Government, Lenders, Shareholders, etc., and finally the environment and society at large. Without being a good corporate citizen, Corporate Governance, however sophisticated it may appear, has no meaning.

Corporate Governance is a key element in improving the economic efficiency of a firm. Further, it ensures that their Board is accountable to the shareholders. This, in turn, helps assure that corporations operate for the benefit of society as a whole. Balancing the interests of all stakeholders alone will ensure survival and growth in the long run. This includes, taking into account societal concerns about labor and the environment.

Corporate Governance Requirements
A perusal of these regulations shows there are elaborate prescriptions about the composition of the Board of Director (including Independent Directors), restrictions on the number of Directorships a Director can hold, kinds of Committees that he can be member of the minimum functional regulations of various committees like Audit Committee, Nomination & Remuneration Committee, Shareholders Grievance Committee, etc. The regulations also prescribe the maximum number of committees a Director can be a member of and also the member of listed companies in which he can be a Director so that focused attention is given by him to his Directorships. The regulations also deal with the different restrictions and disclosures relating to what are known as Related Party Transactions. The regulations also deal with the number and frequency of Board meetings and the minimum information to be placed before the Board of Directors, the adherence to the Company’s Code of Conduct for ethical conduct of business, adherence to vigilance mechanism, the evaluation of the performance of Individual Directors, etc.

Corporate Governance – Insider Trading
One very important area where Corporate Governance has a role to play is in prevention of Insider Trading. It does not require a deep analysis to see that the unscrupulous businessmen, who have always been able to manipulate their way around the system to make huge illegal gains at the cost of innocent investor public. What happens is in the course of managing the Company, the managements in possession of what is called unpublished price sensitive information i.e., information that is essential to the movement of the Company’s share price up or down, but which is known only to few and not to the majority of the investing public.

In the absence of any regulations, the unscrupulous businessmen are likely to mint money by selectively leaking or with holding the information and the gullible public will play into their hands. SEBI can be said to have achieved some degree of success in controlling this evil of Insider Trading by its increased surveillance over price movements in the stock exchanges.

Take over regulations:
Proper and timely disclosure to the capital market of any increased interest evinced by some Investors in acquiring control of companies is ensured in the interest of fair play.

Proxy Advisory Firms- Their Role In Indian Corporate Governance
There are some research entities registered with SEBI who are specialized in the Corporate Governance norms to be complied with by corporate of varying complexities and size. They advise the firms in the areas of enhancing corporate governance practices, educating the firms etc. They also advise share holder bodies on voting recommendations, shareholder activism, provide independent opinions etc.

It’s a sad sight in the Annual General Meetings to see shareholders fighting for gift items and food packets etc. If the shareholders avail themselves of the professional and expert advice offered by these bodies and keep a close watch on the managements, the corporate governance practices will automatically make a

Name of Conference: International Conference on “Paradigm Shift in Taxation, Accounting, Finance and Insurance”
VI. Analysis

**Corporates with good governance – how it affects others:**

[i] Several studies in India and abroad have shown that the investors and capital markets react very positively and favorably towards well managed Companies as perceived by them with higher valuations. The perception that these Companies have proper systems in place, the Boards and Management always go by the rule book and are really independent goes a long way.

[ii] When the members of public are willing to trust a Company with their hard-earned savings, it is only natural that there should be fair play all the way. Otherwise, unscrupulous businessmen are likely to resort to foul means to make a fast buck and vanish.

**The monitoring mechanism:**

The stock exchanges namely Bombay Stock Exchange Ltd. And National Stock Exchange are entrusted with the responsibility of monitoring the compliance of these regulations by the listed companies. Every quarter these companies submit to these exchanges in prescribed forms the details of compliance and the stock exchanges keep a watch over the practices in these companies by going through these forms. However, looking at the compliance reports submitted by the Company to the Stock Exchanges on Corporate Governance if one concludes that there is an effective Corporate Governance in the country, one unhesitatingly is deluding one self. The reason is Corporate Governance in the ultimate analysis is a way of corporate life, rather than a form filling exercise. The existence of Corporate Governance in a Company in its true spirit will be reflected from the high esteem in which it is held by investing world and also by the respect it commands among all the stakeholders viz., the employees, the Government, the suppliers, the creditors and the society at large.

Having said that, the current state of Corporate Governance in the Country is surveyed, there is a sense of disappointed at the present state of Governance.

**Corporate governance – the Indian reality:**

The basic reason for these rather pessimistic observations is the typical Indian tendency to find a way out of any compliance. The native Indian ingenuity to beat any system appears embedded in the DNA of the Indian society. It is interesting to note that the highly qualified, well to do, very famous business people are not immune from this. There is a very well-known colloquial term to describe their state of mind ‘JUGAAD’. What it means is if Corporate Governance is going to be evaluated by the Forms that are submitted to the Stock Exchanges, would not be found wanting. For example, if a Woman Director is to be appointed as required by SEBI, the Promoter will appoint his wife or daughter. It has taken another SEBI appointed Committee to point this out viz., Uday Kotak Committee now to plug this loophole.

The Indian Companies appoint Independent Directors completely satisfying the requirements of regulation, who religiously nod their heads in agreement with the management. The law lays down the definitions of a relative, but the Indian family structure is so varied and wide spread that one can appoint any number of close relatives not falling within the legal definition of a relative.

The violation of Corporate Governance will any way be reflected in the ultimate collapse of the Company but then it will be too late. In this context, one should bear in mind, that the majority of the Indian listed entities are promoter driven with the promoters controlling a majority in the Company. The very fact that SEBI had to appoint so many committees in such short span of around 20 years explains the story.

However, one should not forget that in our country some managements have established a high standard of corporate governance norms in their companies on their own much stricter than SEBI’s. Infosys has been in the news recently. Infosys had set very high norms for itself guided from inception as it has been, by its iconic founder Mr.N.R.Narayana Murthy. It also has been involved in a corporate governance Controversy of a different nature. Following some whistle blower complaints and subsequent enquires the professional management that was running the show [after the founders voluntarily relinquished the management], the Board was absolved of the changes but Shri Murthy was not satisfied and kept making statements that matters were being hushed up etc. The professional management under Mr.Sikka and Mr. Seshasayee left the Company and Mr. Nilekani one of the founders was appointed vice chairman. However, after an enquiry he also arrived at the same conclusion as earlier one.

So, this was a question of how much information was a large shareholder entitled to though not in active management of the Company. Now the latest committee has made some recommendations.
VII. Findings

If one looks further, one can easily realize that the Governance failure is not limited to Corporates. The enormous amounts involved various scams that come to light in the Government, Banks etc., is a clear indication of this attitude towards governance. It is also very obvious that no law in any Country can take care of these aspects. There has to be some self-regulation in all the organs of corporate structure, for instance Auditors. The Finance or Secretarial Auditors who have an important role these days in finalizing the Annual Reports should not hesitate to highlight the irregularities in Companies. What happens among professionals is if any one auditor refuses to certify the accounts there are any others waiting in the wings to take up the assignment; therefore, the management is not afraid of sacking any Auditor and appointing another obliging one. If there is high degree of professional ethics prevalent among the different classes of professionals, the management will never take the professional for granted.

In this context, it is not out of place to mention that even the professionals, who are employed in Companies, turn a blind eye and generally act according to dictates of management. Corporate Governance can never evolve in the proper form, if different professionals do not play their roles properly. For example, every Listed Company certifies that they have a Whistle Blower mechanism in place. What this means is any employee, who is aware of any malpractice in the Company at any level is encouraged to bring this to the notice of Audit Committee and the Audit Committee is expected to enquire and take appropriate action. One can easily imagine in the Indian context, how many workers at the lowest level will have the courage to stand up to the powerful management.

It is only when this right attitude permeates the entire work force as a way of life that the fruits of corporate governance will be enjoyed. While this may sound a utopian ideal, if at least a tangible result is to be achieved, the major organizations dealing with services or with huge financial resources should not be able to get away with errant behavior or with mere compliance with forms.

VIII. Conclusion

In conclusion one can say that there is an increased awareness now-a-days about Corporate Governance. As an example, one can point out the case of Raymond where the attempts of management to buy the Company’s property at low valuation was foiled by the hue and cry raised after the details of the transactions were highlighted in the proper perspective.

If all the stakeholders via; the professionals in employment, those appointed as Independent Directors, the Statutory Auditors, the Secretarial Auditors, the ultimate owners especially the small shareholders, the regulators play their role in a committed way, corporate governance in the Country can certainly see better days to come.

It should also be borne in mind that the state of governance in the entire Federal structure also has a bearing on the corporate governance. If the governance at the political and bureaucratic level reaches higher standards of probity the natural fall out on corporate governance cannot take long to be felt by everybody.