CORPORATE GOVERNANCE IN INDIA: AN EMERGING TREND TOWARDS GLOBAL MARKET ECONOMY

Dr. Abha Mittal
Associate Professor,
Maharaja Agrasen College,
University Of Delhi
Vasundhara Enclave,
Delhi-110096

Ms. Ritika Agarwal
Assistant Professor,
Shyamlal College (M),
University of Delhi

ABSTRACT

Looking at the History of Corporate Governance, the concept cannot be completed without acknowledging the contribution of Kautilya the most celebrated scholar of ancient India. Kaulitya's discussion on administration and management are strikingly modern and scientific covering almost all facets of governance. In the 19th century, state corporation laws enhanced the rights of corporate boards to govern without unanimous consent of shareholders in exchange for statutory benefits like appraisal rights, to make corporate governance more efficient. In this paper we will look at the need of corporate governance, its performance as well as its problems in the Indian context.

INTRODUCTION

To survive and exist in present world of competition which is both healthy and unhealthy, we need to do everything in the best, efficient and effective way. The business world of profit maximization as the sole objective does many kinds of immoral and unethical things. It should also be understood, analyzed, interpreted that the basic purpose of human life is happiness and not necessarily the acquisition of material wealth. We are human beings by birth but to become human capital, we need to utilize our existing spiritual capacities to say no to selfishness. Let corporate sector in the modern world of today learn from Mr. Bill Gates of Microsoft who promotes “Creative Capitalism" as a new avatar of "Trusteeship" of the father of the nation Mahatma Gandhi for improving, adopting and promoting Corporate Social Responsibility (CRS). Willingness to do something for society means all minus myself is necessary and sufficient condition for inclusive growth. Corporate governance, in plain terms, refers to the rules, processes, or laws by which businesses are operated, regulated, and controlled.

The World Bank defines governance as the exercise of political authority and the use of institutional resources to manage society's problems and affairs. India's SEBI Committee on Corporate Governance defines corporate governance as the "acceptance by management of the inalienable rights of shareholders as the true owners of the corporation and of their own role as trustees on behalf of the shareholders. It is about commitment to values, about ethical business conduct and about making a distinction between personal & corporate funds in the management of a company." In simple words thus it can be defined as a process that aims to allocate corporate resources in a manner that maximizes value for all stakeholders – shareholders, investors, employees, customers, suppliers, environment and the community at large and holds those at the helms to account by evaluating their decisions on transparency, inclusivity, equity and responsibility.

Governance, Risk Management, and Compliance or GRC acts as an umbrella term covering an organization's approach across these three areas. While interpreted differently in various organizations, GRC typically encompasses activities such as corporate governance, enterprise risk management (ERM) and corporate compliance with applicable laws and regulations. Governance describes the overall management approach through which senior executives direct and control the entire organization. It ensures that critical management information reaching the executive team is sufficiently complete, accurate and timely to enable appropriate management decision making, and provide the control mechanisms to ensure that strategies, directions and instructions from management are carried out systematically and effectively. Risk management on the other hand, is the set of processes through which management identifies, analyses, and where necessary responds appropriately to risks that might adversely affect realization of the organization's business objectives. Compliance means conforming to stated requirements. At an organizational level, it is achieved through management processes which identify the applicable requirements (defined for example in laws, regulations, contracts, strategies and policies), assess the state of compliance, assess the risks and potential costs of non-compliance against the projected expenses to achieve compliance, and hence prioritize, fund and initiate any corrective actions deemed necessary.

In recent times, corporate governance has received increased attention because of high-profile scandals involving abuse of corporate power and, in some cases, alleged criminal activity by corporate officers, for example the Harshad Mehta stock market scam of 1992. The Satyam Computer Services Scandal was a corporate scandal that occurred in India in 2009 where Chairman Ramalinga Raju confessed that the company's accounts had been falsified. The Rs. 7,000 crore frauds wiped off $2 billion worth shareholders wealth in the week. It exposed glaring shortcomings of corporate governance, threatening India's appeal to foreign investors.

Cumbersome procedures of doing business of any kind are the examples of bad governance. Mismanagement of the budget and financial resources exists at all levels of government. The basic reason for failure of corporate governance regulation is that it is based on a box ticking approach of compliance. This encourages companies using their ingenuity in HNTGC – How Not to Get Caught. Human ingenuity is so powerful that we always find excuses to beat the system. In fact our manhood depends on our ability to defy rules. You become a master only by transcending rules which most read as transgressing rules. The basis reason is that rules are devised to meet a certain situation and not supposed to be permanent. Hence there is a tendency to interpret them to suit your own convenience. Principles on the other hand are North Star fixed for all times with no scope for ambivalence. A strategy for sustainability requires we apply a principle=based approach to corporate governance. The basic purpose of corporate governance is to hold those in power to account. So accountability is the key to corporate governance. There are 6 principles that have to be satisfied to ensure accountability. These are 6 D's – Diversity in composition of the board and differentiating the gene pool and gender; encouragement of Dialogue as opposed to monologue; valuing Dissent, Dispersion of authority (separation of chairman and CEO is one example), disruption of status quo (critical to counter cosines) and fostering a culture of full disclosure to build trust.

Corporate Governance mechanisms and controls are designed to reduce the inefficiencies that arise from moral hazard and adverse selection. For example, to monitor manager's behavior, an independent third party (the auditor) attests the accuracy of information provided by management to investors. An ideal control system should regulate both motivation and ability. Good corporate governance helps an organization achieve several objectives like a) Developing appropriate strategies that result in the achievement of stakeholder objectives b) Attracting, motivating and retaining talent c)Creating a secure and prosperous operating environment and improving operational performance d) Managing and mitigating risk and protecting and enhancing the company's reputation.

The main players in the area of corporate governance can be classified into two groups namely internal and external. Internal Corporate Governance controls and monitor activities and then take corrective action to accomplish organizational goals. The board with its legal authorities hire, fire and compensate top management, safeguards invested capital. Regular board meetings allow potential problems to be identified, discussed and avoided. External Corporate Governance on the other hand, controls external stakeholders exercise over the organization, debt covenants, Government regulations, media pressure, competition etc. Through Corporate Social Responsibility (CSR) organizations consider the interests of society by taking responsibility for the impact their activities have on customers, suppliers, employees, communities and the environment. This responsibility goes beyond compliance with regulations and is about organizations voluntarily taking further steps to improve the quality of life for employees as well as for the local community and society at large

There are many different models of corporate governance around the world. These differ according to the variety of capitalism in which they are embedded. The Anglo-American "model" tends to emphasize the interests of shareholders. The coordinated or Multi-stakeholder Model associated with Continental Europe and Japan also recognizes the interests of workers, managers, suppliers, customers, and the community. A related distinction is between market-orientated and network-orientated models of corporate governance.

Corporate governance principles and codes have been developed in different countries and issued from stock exchanges, corporations, institutional investors, or associations (institutes) of directors and managers with the support of governments and international organizations. As a rule, compliance with these governance recommendations is not mandated by law, although the codes linked to stock exchange listing requirements may have a coercive effect.

Basic Principles on which good Corporate Governance is based is to make sure that all shareholders get a voice at general meetings and are allowed to participate. Taking the time to address non-shareholder stakeholders can help the company establish a positive relationship with the community and the press. Ethical behavior violations in favor of higher profits can cause massive civil and legal problems down the road. Underpaying and abusing outsourced employees or skirting around lax environmental regulations can come back and bite the company hard if ignored. A code of conduct regarding ethical decisions should be established for all members of the board. Business transparency is the key to promoting shareholder trust. Financial records, earnings reports and forward guidance should all be clearly stated without exaggeration or “creative” accounting. Falsified financial records can cause your company to become a Ponzi scheme, and will be dealt with accordingly.

OECD principles published in 1999 and revised in 2004, are often referred by countries developing local codes or guidelines. Building on the work of the OECD, other international organizations, private sector associations and more than 20 national corporate governance codes, the United Nations Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting (ISAR) has produced their Guidance on Good Practices in Corporate Governance Disclosure. This internationally agreed benchmark consists of more than fifty distinct disclosure items across five broad categories:

- Auditing
- Board and management structure and process
- Corporate responsibility and compliance in organization
- Financial transparency and information disclosure
- Ownership structure and exercise of control rights

According to the Stock exchange listing standards, Companies listed on the New York Stock Exchange (NYSE) and other stock exchanges are required to meet certain governance standards. For example, the NYSE Listed Company Manual requires, among many other elements:

- Independent directors: "Listed companies must have a majority of independent directors...Effective boards of directors exercise independent judgment in carrying out their responsibilities. Requiring a majority of independent directors will increase the quality of board oversight and lessen the possibility of damaging conflicts of interest." (Section 303A.01) An independent director is not part of management and has no "material financial relationship" with the company.
- Board meetings that exclude management: "To empower non-management directors to serve as a more effective check on management, the non-management

directors of each listed company must meet at regularly scheduled executive sessions without management." (Section 303A.03)

- Boards organize their members into committees with specific responsibilities per defined charters. "Listed companies must have a nominating/corporate governance committee composed entirely of independent directors." This committee is responsible for nominating new members for the board of directors. Compensation and Audit Committees are also specified, with the latter subject to a variety of listing standards as well as outside regulations. (Section 303A.04 and others)

Key parties involved in corporate governance include stakeholders such as the board of directors, management and shareholders. External stakeholders such as creditors, auditors, customers, suppliers, government agencies, and the community at large also exert influence. The agency view of the corporation posits that the shareholder forgoes decision rights (control) and entrusts the manager to act in the shareholders' best (joint) interests. The board is responsible for the successful perpetuation of the corporation which cannot be relegated to management. A Board of Directors is expected to play a key role in corporate governance. The board has responsibility for: CEO selection and succession; providing feedback to management on the organization's strategy; compensating senior executives; monitoring financial health, performance and risk; and ensuring accountability of the organization to its investors and authorities.

All parties to corporate governance have an interest, whether direct or indirect, in the financial performance of the corporation. Directors, workers and management receive salaries, benefits and reputation, while investors expect to receive financial returns. For lenders, it is specified interest payments, while returns to equity investors arise from dividend distributions or capital gains on their stock. Customers are concerned with the certainty of the provision of goods and services of an appropriate quality; suppliers are concerned with compensation for their goods or services, and possible continued trading relationships. These parties provide value to the corporation in the form of financial, physical, human and other forms of capital

The single most important development in the field of corporate governance and investor protection in India has been the establishment of the SEBI in 1992 and its gradual and growing empowerment since then. Established primarily to regulate and monitor stock trading, it has played a crucial role in establishing the basic minimum ground rules of corporate conduct in the country. These concerns about corporate governance stemming from the corporate scandals, coupled with a perceived need of opening up the corporate sector to the forces of competition and globalization gave rise to several investigations into ways to fix the corporate governance situation in India. One of the first such endeavors was the Confederation of Indian Industry (CII) Code for Desirable Corporate Governance, developed by a committee chaired by Rahul Bajaj in 1996. The objective was to develop and promote a code for corporate governance to be adopted and followed by Indian companies, be the Private Sector, the Public Sector, Banks or Financial Institutions, all of which are corporate entities. This initiative by CII flowed from public concerns regarding the protection of investor interest, especially the small investor, the promotion of transparency within business and industry.

SEBI asked Indian firms above a certain size to implement Clause 49 of the Listing agreement of SEBI Act which is an outcome of Narayana Murthy Committee (2006). It is a regulation that strengthens the role of independent directors serving on corporate boards and enhances the corporate governance (CG) requirements, primarily through increasing the responsibilities of the Board, consolidating the role of the Audit Committee and making management more accountable.

Jayati Sarkar and Subrata Sarkar show that corporate boards of large companies in India in 2003 were slightly smaller than those in the United States in 1991, with 9.46 members on average in India compared to 11.45 in America. While the percentage of inside directors were comparable (25.38% compared to 26% in the U.S), Indian boards had relatively fewer independent directors, 54% compared to 60% in U.S. there is evidence that larger boards lead to poorer performance both in India and in the United States.

SEBI has also taken a number of initiatives in the area of investor protection. For example, just like company law SEBI has added substantially to information disclosure in both prospectuses and in annual accounts. Another aspect of the SEBI regulations is that in most public issues, the promoters (typically the dominant shareholders) are required to take a minimum stake of about 20% in the capital of the company and to retain these shares for a minimum lock-in period of about three years. However, the SEBI regulations provide an exemption to those companies where there is no identifiable promoter group, that is to say, no dominant shareholder. Moreover, SEBI has intervened to tackle the dominant shareholder in the pricing rule that it has imposed on preferential allotments. Company law itself provides that new issue of shares must be rights issues to existing shareholders unless the shareholders in general meeting allow the company to issue shares to the general public or to other parties. In 1994, SEBI issued new guidelines on preferential allotment that prohibited preferential allotments at a price lower than the average market price during the last six months.

This regulatory intervention illustrates very nicely the problems that the regulator faces in dealing with governance abuses by the dominant shareholder. There are many situations where it may be in the interests of the company as a whole (and not just the dominant shareholders) to issue equity at below the six monthly average prices.

CONCLUSION

It is concluded that whatever be the approach towards corporate governance by private sector companies or public sector companies in India or any organization in any country of the world, the aim remains the same of managing the affairs of the company in way that ensures transparency, accountability and fairness in all its transactions with the ultimate focus on enhancement of long term value creation for all its stakeholders without compromising on integrity, social obligations, environmental and regulatory compliances. The importance of corporate governance lies in its contribution both to business prosperity and accountability. Good corporate governance stimulates performance, generating higher returns and profitability of companies, leads to higher total factor productivity growth, a major source of economic growth. The systematic problems of the corporate governance are: demand for information, which arises in order to influence the directors, the shareholders must combine with others to form a voting group which can pose a real threat of carrying resolutions or appointing directors at a general meeting. Supply of accounting information - Financial accounts form a crucial link in enabling providers of finance to monitor directors. Imperfections in the financial reporting process will cause imperfections in the effectiveness of corporate governance. This should, ideally, be corrected by the working of the external auditing process. Thus, the key to better corporate governance today lies in a more efficient and healthy relation between manager and shareholder. The failure of a company to establish an effective system of corporate governance represents a major operational risk to the company and its investors. Last but not the least an effective corporate governance systems promote the development of strong financial systems-irrespective of whether they are largely bank- based or market-based –which, in turn, have an unmistakably positive effect on economic growth and poverty reduction.

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