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Corporate Governance in India: Concept, Needs And Principles Special Reference To Chennai

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ABSTRACT

Corporate Governance is the set of policies that are created for deciding a company's performance and direction. It is an overview of rules and regulations for the people in-charge of an incorporated firm. They are the ones who agree to take responsibility towards the shareholders. Corporate governance is a broad term is today's business environment. Corporate governance is a multidisciplinary field of study it covers a wide range of disciplines – accounting, consulting, economics, ethics, finance, law, and management. However, fact of the matter is that the observance of practices of good corporate governance will ensure investors' confidence in the companies which have record of good corporate governance. This paper highlights the Concepts, need for corporate governance, Principles, SEBI's guidelines and Regulatory framework of Corporate Governance in India.

INTRODUCTION

In the context of liberalization and globalization, there is growing realization in the emerging economies including India that a country's business environment must be maintained and operated in a manner that is conducive to investors' confidence, so that both domestic and foreign investors are induced to make adequate investment in corporate companies. This will be conducive to rapid capital formation and sustained growth of the economy. The need for corporate governance is, then, imperative for reviving investors' confidence in the corporate sector towards the economic development of society.

CONCEPT OF CORPORATE GOVERNANCE

Corporate governance refers to the accountability of the Board of Directors to all stakeholders of the corporation i.e. shareholders, employees, suppliers, customers and society in general; towards giving the corporation a fair, efficient and transparent administration. "Corporate governance means that company manages its business in a manner that is accountable and responsible to the shareholders. Corporate governance is more than company administration. It refers to a fair, efficient and transparent functioning of the corporate management system. It refers to a code of conduct; the Board of Directors must abide by; while running the corporate enterprise. Corporate governance refers to a set of systems, procedures and practices which ensure that the company is managed in the best interest of all corporate stakeholders.

NEED FOR CORPORATE GOVERNANCE:

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(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 unorganized 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 the 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 events of Harshad Mehta scandal, Sathyam Computers, are in the heart and mind of all, connected with corporate shareholding or otherwise being educated and socially conscious.

(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 utilization 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-over's of corporations witnessed in several countries, put a question mark on the efficiency of managements of take-over companies. This factor 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) GLOBALIZATION:

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

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in the corporate sector. There is no doubt that international capital market recognizes only companies well-managed according to standard codes of corporate governance.

PRINCIPLES OF CORPORATE GOVERNANCE:

(I) TRANSPARENCY:
Transparency means the quality of something which enables one to understand the truth easily. In the context of corporate governance, it implies an accurate, adequate and timely disclosure of Relevant information about the operating results etc. of the corporate enterprise to the stake holders. In fact, transparency is the foundation of corporate governance; which helps to develop a high level of public confidence in the corporate sector. For ensuring transparency in corporate administration, a company should publish relevant information about corporate affairs in leading newspapers, e.g., on a quarterly or half yearly or annual basis.

(II) ACCOUNTABILITY:
Accountability is a liability to explain the results of one's decisions taken in the interest of others. In the context of corporate governance, accountability implies the responsibility of the Chairman, the Board of Directors and the chief executive for the use of company's resources (over which they have authority) in the best interest of company and its stakeholders.

(III) INDEPENDENCE:
Good corporate governance requires independence on the part of the top management of the corporation i.e. the Board of Directors must be strong non-partisan body; so that it can take all corporate decisions based on business prudence. Without the top management of the company being independent; good corporate governance is only a mere dream.

SEBI CODE OF CORPORATE GOVERNANCE:
To promote good corporate governance, SEBI (Securities and Exchange Board of India) constituted a committee on corporate governance under the chairmanship of Kumar Mangalam Birla. On the basis of the recommendations of this committee, SEBI issued certain guidelines on corporate governance; which are required to be incorporated in the listing agreement between the company and the stock exchange.

AN OVERVIEW OF SEBI GUIDELINES ON CORPORATE GOVERNANCE IS GIVEN BELOW, UNDER APPROPRIATE HEADS:

(A) BOARD OF DIRECTORS:

- The Board of Directors of the company shall have an optimum combination of executive and non-executive directors.
- The number of independent directors would depend on whether the chairman is executive or non-executive.

In case of non-executive chairman, at least, one third of the Board should comprise of independent directors; and in case of executive chairman, at least, half of the Board should comprise of independent directors. The expression 'independent directors' means directors, who apart from receiving director's remuneration, do not have any other material pecuniary relationship with the company.

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(B) AUDIT COMMITTEE:

THE COMPANY SHALL FORM AN INDEPENDENT AUDIT COMMITTEE WHOSE CONSTITUTION WOULD BE AS FOLLOWS:

- It shall have minimum three members, all being non-executive directors, with the majority of them being independent, and at least one director having financial and accounting knowledge.

- The Chairman of the committee will be an independent director.
- The Chairman shall be present at the Annual General Meeting to answer shareholders' queries.

THE AUDIT COMMITTEE SHALL HAVE POWERS WHICH SHOULD INCLUDE THE FOLLOWING:

- 1.To investigate any activity within its terms of reference
- 2.To seek information from any employee
- 3. To obtain outside legal or other professional advice
- 4. To secure attendance of outsiders with relevant expertise, if considered necessary.

(3) THE ROLE OF AUDIT COMMITTEE SHOULD INCLUDE THE FOLLOWING:

- Overseeing of the company's financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct, sufficient and credible.
- Recommending the appointment and removal of external auditor.
- Reviewing the adequacy of internal audit function
- Discussing with external auditors, before the audit commences, the nature and scope of audit; as well as to have post-audit discussion to ascertain any area of concern.
- Reviewing the company's financial and risk management policies.

(C) REMUNERATION OF DIRECTORS:

- All elements of remuneration package of all the directors i.e. salary, benefits, bonus, stock options, pension etc.
- Details of fixed component and performance linked incentives, along with performance criteria.

(D) BOARD PROCEDURE SOME POINTS IN THIS REGARDS ARE:

- Board meetings shall be held at least, four times a year, with a maximum gap of 4 months between any two meetings.
- A director shall not be a member of more than 10 committees or act as chairman of more than five committees, across all companies, in which he is a director.

(E) MANAGEMENT:

A Management Discussion and Analysis Report should form part of the annual report to the shareholders; containing discussion on the following matters (within the limits set by the company's competitive position).

(i) Opportunities and threats
(ii) Segment-wise or product-wise performance
(iii) Risks and concerns

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(iv) Discussion on financial performance with respect to operational performance
(v) Material development in human resource/industrial relations front.

(F) SHAREHOLDERS:
(I) IN CASE OF APPOINTMENT OF A NEW DIRECTOR OR REAPPOINTMENT OF A DIRECTOR, SHAREHOLDERS MUST BE PROVIDED WITH THE FOLLOWING INFORMATION:

- A brief resume (summary) of the director
- Nature of his expertise
- Number of companies in which he holds the directorship and membership of committees of the Board.

(ii) A Board Committee under the chairmanship of non-executive director shall be formed to specifically look into the redressing of shareholders and investors' complaints like transfer of shares, non-receipt of Balance Sheet or declared dividends etc. This committee shall be designated as 'Shareholders / Investors Grievance Committee'.

(G) REPORT ON CORPORATE GOVERNANCE:
There shall be a separate section on corporate governance in the Annual Report of the company, with a detailed report on corporate governance.

(H) COMPLIANCE:
The company shall obtain a certificate from the auditors of the company regarding the compliance of conditions of corporate governance. This certificate shall be annexed with the Directors' Report sent to shareholders and also sent to the stock exchange.

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** 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

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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.

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

- New Companies Act introduces significant changes to the composition of the boards of directors.
- 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.
    - New Companies Act mandates following committees to be constituted by the board for prescribed class of company
    - Audit committee
    - Nomination and remuneration committee
    - Stakeholders relationship committee
    - Corporate social responsibility committee

CONCLUSION

It is evident from above that it is essential that good governance practices must be effectively implemented and enforced preferably by self-regulation and voluntary adoption of ethical code of business conduct. The effective implementation of good governance practices would ensure investors confidence in the corporate companies which will lead to greater investment in them ensuring their sustained growth. Thus good corporate governance would greatly benefit the companies enabling them to thrive and prosper. In fact in good corporate governance structure what is ensured is that companies must preferably follow voluntarily ethical code of business conduct which are conducive to the expansion of investment in them and ensure good outcome in terms of rates of return.

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