CORPORATE GOVERNANCE IN INDIA-EVOLUTION AND CHALLENGES

Dr. K.Babu Rajendra Prasad

Assist. Professor of Political Science
Government First Grade College,
Mariyammanahalli-583222

"Good corporate governance is about 'intellectual honesty' and not just sticking to rules and regulations, capital flowed towards companies that practised this type of good governance"
- Mervyn King

Abstract

"The present paper aims at reviewing the various developments in Corporate Governance in India. The emergence of new technologies in the era of globalisation and liberalisation entirely changedthe nature of business transactions. By the evolution of business life cycles business transactions became very complex and managing risk became a challenging task for the organisations. Concerns about corporate governance in India were, however, largely triggered by Harshad Mehta stock market scam of 1992 followed by incidents of companies allotting preferential shares to their promoters at deeply discounted prices and the recent scam of sathyam. Good corporate governance became a key word to handle accounting scandals and to mitigate growingconcern about the quality of financial statements. In short Corporate Governance is about promoting corporate fairness, transparency and accountability."

Keywords: Corporate, governance, globalization, liberalization.

Introduction:

Corporate Governance is essentially all about howcorporations are directed, managed, controlled and heldaccountable to their shareholders. In India, the question ofCorporate Governance has come up mainly in the wake ofeconomic liberalization and de-regularization of industry andbusiness. With the rapid pace of globalization manycompanies have been forced to tap international financialmarkets and consequently to face greater competition thanbefore. Both policymakers and business managers havebecome increasingly aware of the importance of improvedstandards of Corporate Governance.India has one of the best corporate governance laws but poor implementation together with socialistic policies of the prereform era has affected corporate governance. Concentrated ownership of shares, pyramiding and tunneling of funds among group companies mark the Indian corporate landscape.

Significance:

A corporation is a congregation of various stakeholders, namely customers, employees, investors, vendor partners, government and society. In this changed scenario an Indian corporation, as also a corporation elsewhere, should be fair and transparent to its stakeholders in all its transactions. This has become imperative in today's globalized business world where corporations need to access global pools of capital, need to attract and retain the best human capital from various parts of the world, need to partner with vendors on mega collaborations and need to live in harmony with the community. Unless a corporation embraces and demonstrates ethical conduct, it will not be able to succeed. Corporations need to recognize that their growth requires the cooperation of all the stakeholders; and such cooperation is enhanced by the corporations adhering to the best Corporate Governance practices

Objectives:

1.To know the evolution of corporate governance.

2.The Present paper is basically concerned with the Issues andChallenges for Corporate Governance in India.

3.The paper also analyses regulatorydeficiencies in corporate governance.

4.To provide suggestions bases on study.

Research Methodology:

Looking into requirements of the objectives of the study the research design employed forthe study is of descriptive type. Available secondary data was broadly used for the study. The investigator procured therequired data through secondary survey method. Different news articles, Books and Webwere used which were enumerated and recorded.

Meaning:

Definition of Corporate Governance varies widely.The concept of "governance" is not new. It is as old as human civilization. Simply put "governance" means: the process of decision-making and the process by which decisions are implemented (or not implemented). Governance can be used in several contexts such as corporate governance, international governance, national governance and local governance. It is participatory, consensus oriented, accountable, transparent, responsive, effective and efficient, equitable and inclusive and follows the rule of law. It assures that corruption is minimized, the views of minorities are taken into account and that the voices of the most vulnerable in society are heard in decision-making. It is also responsive to the present and future needs of society.

Evolution of Corporatre Governance in India:

The concept of good governance is very old in India dating back to third century B.C. where Chanakya (Vazir of Parliputra) elaborated fourfold duties of a king viz. Raksha, Vriddhi, Palana and Yogakshema. Substituting the king of the State with the Company CEO or Board of Directors the principles of Corporate Governance refers to protecting shareholders wealth (Raksha), enhancing the wealth by proper utilization of assets (Vriddhi), maintenance of wealth through profitable ventures (Palana) and above all safeguarding the interests of the shareholders (Yogakshema or safeguard). Corporate Governance was not in agenda of Indian Companies until early 1990s and no one would find much reference to this subject in book of law till then. In India, weakness in the system such as undesirable stock market practices, boards of directors without adequate fiduciary responsibilities, poor disclosure practices, lack of transparency and chronic capitalism were all crying for reforms and improved governance. The fiscal crisis of 1991 and resulting need to approach the IMF induced the Government to adopt reformative actions for economic stabilization through liberalization. The momentum gathered albeit slowly once the economy was pushed open and the liberalization process got initiated in early 1990s. As a part of liberalization process, in 1999 the

Government amended the Companies Act, 1956. Further amendments have followed subsequently in the year 2000, 2002 and 2003.The major corporate governance initiatives launched in India since the mid 1990s.There are various reformswhich were channelled through a number of different pathswith both the Security and Exchange Board of India **(SEBI)**and the Ministry of Corporate Affairs, Government of India(MCA) playing important roles.

A.Committee on Corporate Governance

Reforming the Corporate Governance in India since **1990s.**

1. Confederation of Indian Industries (CII):

The Confederaton of Indian Industries is set up a taskforce in 1995 under Rahul Bajaj, a reputedindustrialist. In April 1998, the CII released the code called"Desirable Corporate Governance". It looked intovarious aspects of Corporate Governance and wasfirst to criticize nominee directors and suggesteddilution of government stake in companies

2. Kumar Mangalam Birla Committee Report

While the CII code was well received by corporate sector and some progressive companies also adopted it, it was felt that under Indian conditions a statutory rather than a voluntary code would be more meaningful. Consequently the second major initiative was undertaken by the Securities and Exchange Board of India (SEBI) which set up a committee under the chairmanship of Kumar Mangalam Birla in 1999 with the objective of promoting and raising of standards of good corporate governance. In early 2000 the SEBI Board accepted and ratified the key recommendations of this committee and these were incorporated into Clause – 49 of the Listing Agreement of the Stock Exchanges.

3.Department of Corporate Affairs (DCA)

In May 2000, the Department of Corporate Affairs (DCA) formed a broad based study group under the chairmanship of Dr. P.L. Sanjeev Reddy, Secretary of DCA. The group was given the ambitious task of examining ways to "operationalise the concept of corporate excellence on a sustained basis" so as to "sharpen India's global competitive edge and to further develop corporate culture in the country". In November 2000 the Task Force on Corporate Excellence set up by the group produced a report containing a range of recommendations for raising governance standards among all companies in India.

4.Naresh Chandra Committee Report

A committee was appointed by Ministry of Finance and Company Affairs in August 2002 under the chairmanship of Naresh Chandra to examine and recommend inter alia amendments to the law involving the auditor-client relationships and the role of independent directors. The committee made recommendations in two key aspects of corporate governance: financial and non-financial disclosures: and independent auditing and board oversight of management.

5.Narayana Murthy Committee Report in 2002

The SEBI constituted a committee under the chairmanship of Narayana Murthy for reviewing implementation of the corporate governance code by listed companies and issue of revised clause 49. Some of the major recommendations of the committee primarily related to audit committees, audit reports, independent directors, related party transactions, risk management, directorships and director compensation, codes of conduct and financial disclosures.

Clause 49 of the Listing Agreement

After liberalization serious efforts have been made towards overhauling the system with SEBI formulating the Clause 49 of the Listing Agreements dealing with corporate governance. Clause 49 of the Listing Agreement to the Indian stock exchange comes into effect from 31 December 2005**.** It includes the following key requirements:

• Board Independence: Boards of directors of listedcompanies must have a minimum number of independent directors.

• Audit Committees: Listed companies must have audit committees of the board with a minimum of three directors, two-thirds of whom must be independent.

• Disclosure: Listed companies must periodically make various disclosures regarding financial and other matters to ensure transparency.

6.J.J. Irani Committee Report

The Companies Act 1956 was enacted on the recommendations of the Bhaba Committee set up in 1950 with the object to consolidate the existing corporate laws and to provide a new basis for corporate operation in independent India. With enactment of this legislation in 1956 the Companies Act 1913 was repealed. The need for streamlining this Act was felt from time to time as the corporate sector grew in pace with the Indian economy and as many as 24 amendments have taken place since 1956. The major amendments to the Act were made through Companies (Amendment) Act 1998 after considering the recommendations of Sachar Committee followed by further amendments in 1999, 2000, 2002 and finally in 2003 through the Companies (Ammendment) Bill 2003 pursuant to the report of R.D. Joshi Committee. After a hesitant beginning in 1980, India took up its economic reforms programme in 1990s and a need was felt for a comprehensive review of the Companies Act 1956. The Government therefore took a fresh initiative in this regard and constituted a committee in December 2004 under the chairmanship of Dr. J.J. Irani with the task of advising the government on the proposed revisions to the Companies Act 1956.

7.Central Coordination and Monitoring Committee

A high powered Central Coordination and Monitoring Committee (CCMC) co-chaired by Secretary, Department of Corporate Affairs' and Chairman, SEBI was set up by the Department of Corporate Affairs to monitor the action taken against the vanishing companies and unscrupulous promoters who imsused the funds raised from the public. It was decided by this committee that seven Task Forces be set up at Mumbai, Delhi, Chennai, Kolkata, Ahmedabad, Bangalore and Hyderabad.

8.National Foundation of Corporate Governance

Recently the Ministry of Company Affairs has set up National Foundation for Corporate Governance (NFCG) in association with Confederation of Indian Industry (CII), Institute of Company Secretaries of India (ICSI) and Institute of Chartered Accountants of India (ICAI).

9.*Voluntary Guidelines issued by Ministry of CorporateAffairs*

Voluntary Guidelines on Corporate Governance wereissued by the **Ministry of Corporate Affairs in December2009**. Few guidelines are worth mentioning.

• The offices of chairman of the board and chiefexecutive officer should be separate.• The companies may have a Nomination Committeecomprised of a majority of Independent Directors,including its Chairman.• Independent Directors should not be paid with stockoptions or profit-based commission.• The Board should provide training for the directors.• The Audit Committee should be composed of at leastthree members, with Independent Directors in themajority and an Independent Director as thechairperson.• The audit partner should be rotated every three years;the firm should be rotated every five years. • The Committee may appoint an internal auditor.

10. Ownership structure

There are two sets of issues pertaining to the ownership structure of the listed companies in India. First, there is high concentration of ownership, which gives particular individuals or families actual or effective control of most companies, even publicly traded companies Second, a large number of companies in India are grouped together under the common control of a single shareholder or family.

11.Establishment of the NSE Centre for Excellence in Corporate Governance

To encourage best standards of corporate governance among the Indian corporates and to keep them abreast of the emerging and existing issues, the NSE set up in December, 2012, a Centre for Excellence in Corporate Governance (NSE CECG). This is an independent expert advisorybody comprising eminent domain experts, academics and practitioners.

12. Corporate Governance provisions in the Companies Act, 2013.

The enactment of the companies Act 2013 was major development in corporate governance in 2013. The new Act replaces the Companies Act, 1956 and aims to improve corporate governance standards, simplify regulations and enhance the interests of minority shareholders.

i. *Board of Directors (Clause 166):* The new Act provides that the company can have a maximum of 15 directors on the Board;

ii. *Independent Director (Clause 149):* The concept of independent directors (IDs) has been introduced for the first time in the Company Law in India.

iii. *Related Party Transactions (RPT) (Clause 188):* The new Act requires that no company should enter into RPT contracts pertaining to sale, purchase or supply of any goods or materials

iv. *Corporate Social Responsibility (CSR) (Clause 135):* The new Act has mandated the profit making companies to spend on CSR related activities

v. *Auditors (Clause 139):* A listed company cannot appoint or reappoint (a) an individual as auditor for more than one term of five consecutive years,

vi. *Disclosure and Reporting (Clause 92):* In the new Act, there is significant transformation in non-financial annual disclosures and reporting by companies as compared to the earlier format in the Companies Act, 1956.

vii. *Class action suits (Clause 245):* For the first time, a provision has been made for class action under which the order passed by the Tribunal shall be binding on all the stakeholders including the company and all its members, depositors and auditors.

Challenges & Imperatives:

1.A corporation should be fair and transparent to its stakeholders in all its transactions. This has become imperative in today's globalized business world where corporations need to access global pools of capital, need to attract and retain the best human capital from various parts of the world.Unless a corporation embraces and demonstrates ethical conduct, it will not be able to succeed.

2. What is "Corporate Governance " It is known fact that vital needs of success of any organization lingers on its ability to mobilize and utilize all kinds of resources to meet the objectives clearly set as part of the planning process.

3. Corporate governance is about ethical conduct in business. Ethics is concerned with the code of values and principles that enables a person to choose between right and wrong. Further, ethical dilemmas arise from conflicting interests of the parties involved.

4.It is quite possible that in the effort at arriving the best possible financial results or business results there could be attempts at doing things which are verging on the illegal or even illegal. There is also the possibility of grey areas where an act is not illegal but considered unethical. These raise moral issues.

5. The rapid migration of four elements across national borders. These are (i) Physical capital in terms of plant and machinery; (ii) Financial capital; (iii) Technology; and (iv) Labour.

6. Strong corporate governance is indispensable to resilient and vibrant capital markets and is an important instrument of investor protection.

7. Companies raise capital from market and investors suffered due to unscrupulous managements that performed much worse than past reported figures. Many corporates did not pay heed to investors' grievances

8. Theboard of directors and the senior level management ofan enterprise - walking their talk. It is by walking their talk that the top management can earn credibility. This also has a direct bearing on the morale of an organisation.

9. When it comes to the hardware aspect of corporate governance, we go into the issue of a code, which becomes a reference point for behaviour. But the sad fact in our country is that even though there is a lot of talk about corporate governance, when it comes to reality, nothing much happens.

10. In the Indian context lack of transparency that leads to corrupt or illegal behaviour.

11.Perhaps the most important challenge we face towards better corporate governance is the mindset of the people and the organisational culture. This change will have to come from within.

12. Another important aspect is to realise that ultimately the spirit of corporate governance is more important than the form. Substance is more important than style. Values are the essence of corporate governance and these will have to be clearly articulated and systems and procedures devised, so that these values are practiced.

13. We then come to a common moral problem in running enterprises. One can have practices which are legal but which are unethical. In fact, many a time, tax planning exercises may border on the fine razor's edge between the strictly legal and the patently unethical.

14. Openness, integrity and accountability are the key elements of Corporate Governance for any corporate entity. These factors assume greater importance in case of Public Sector Banks.

15. Banks deal in trust. If trust is in suspicion, damaged or lost, the resulting financial loss cannot measure the true risk. Trust being the foundation of banking, the discussion over applicability of good governance has really been a non-issue

16. The report of the Consultative Group of Directors of Banks/Financial Institutions – chaired by A.S. Ganguly has focussed on more fundamental issues like the supervisory role of boards of banks and financial institutions and functioning of the boards vis-à-vis compliance, transparency, disclosures, audit committees etc.

17. Ethics in managing an organisation are vital for long term survival. As far as business ethics are concerned, a minimum code of ethics has to be practiced in competition, public relations and social responsibilities. Corporate Governance encourages ethical standards and sound business practices.

18. Corporate governance extends beyond corporate law. Its objective is not mere fulfilment of legal requirements but ensuring commitment on managing transparently for maximising shareholder values.

19. Finally, transparency about a company's governance process is critical. Implementing Corporate Governance structures are Important but instilling the right culture – work culture is Most Essential.

Suggestions:

1. Value based corporate culture: For any organization to run in effective way, it needs tohave certain ethics, values. Long run business needs to have based corporate culture. It is a set ofbeliefs, ethics, principles which are inviolable

2. Holistic view: This holistic view is more or less godly, religious attitude which helps inrunning organization. It is not easier to adopt it, it needs special efforts and once adoptedit leads to developing qualities of nobility, tolerance and empathy.

3. Compliance with laws: Those companies abide and comply with laws of SecuritiesExchange Board of India (SEBI), Foreign Exchange Regulation Act, Competition Act2002, Cyber Laws, Banking Laws etc.

4. Disclosure, transparency, and accountability: Disclosure, transparency and accountabilityare important aspect for good governance. Timely and accurate information should bedisclosed on the matters like the financial position, performance etc. Due to tremendous competitionin the market place the customers having choices don't shift to other corporate bodies.

5. Corporate Governance and Human Resource Management: For any corporate body,the employees and staff are just like family. For a company to be perfect the role ofHuman Resource Management becomes very vital, they both are directly linked. Everyindividual should be treated with individual respect, his achievements should berecognized. Each individual staff and employee should be given best opportunities toprove their worth and these can be done by Human Resource Department.

6. Innovation: Every Corporate body needs to take risk of innovation i.e. innovation inproducts, in services and it plays a pivotal role in corporate governance.

7. Necessity of Judicial Reform: There is necessity of judicial reform for a good economyand also in today's changing time of globalization and liberalization. It needs to speedily resolve disputes in cost effectivemanner.

8. Lessons from Corporate Failure: Every story has a moral to learn from, every failurehas success to learn from, in the same way, corporate body have certain policies whichif goes as a failure they need to learn from it. Failure can be both internal as well asexternal whatever it may be, in good governance, corporate bodies need to learn fromtheir failures and need to move to the path of success.

9.Independent directors- selection criteria must be transparent, also process of appointment ofBOD must be reconsidered.

10. It is important to focus on not just Quantity or profits but on the sustainability of businessmodels.

11.Need for having supervising the functions of management and make them accountable andtransparent to shareholders.

12.Codes of conduct and whistle blower policies must be framed in such a way as to be possibleto put in to practise.

13 Regulators should enhance penalities as well as to fix liability in imposing substantial penaltiesfor non-compliance,

Conclusion:

The concept of corporate governance hinges on total transparency, integrity and accountability of the management and the board of directors. Be it finance, taxation, banking or legal framework each and every place requires good corporate governance. Corporate Governance is a means not an end, Corporate Excellence should be the end. Once, the good Corporate Governance is achieved and the Indian Corporate Body will shine to outshine the whole world. In the Indian context, the need for corporate overnance has been highlighted because of the scams occurring frequently since the emergence of the concept of liberalisation from 1991. We had the Harshad Mehta Scam, Ketan Parikh Scam, UTI Scam, Vansishing Company Scam, Bhansali Scam and so on. In the Indian corporate scene, there is a need to induct global standards so that at least while the scope for scams may still exist, it can be at least reduced to the minimum. Corporate governance and ethical behavior have a number of advantages. Firstly, they help to build good brand image for the company. Once there is a brand image, there is greater loyalty, once there is greater loyalty, there is greater commitment to the employees, and when there is a commitment to employees, the employees will become more creative. In the current competitive environment, creativity is vital to get a competitive edge. Corporate Governance in the Public Sector cannot be avoided and for this reason it must be embraced. But Corporate Governance should be embraced because it has much to offer to the Public Sector. Good Corporate Governance, Good Government and Good Business go hand in hand.

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