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An Indian View of Corporate Governance

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Abstract: *Corporate governance is the most enhanced and important tool as on date, corporates have committed many scams worldwide and in India as well with the inclusion of companies act 2013 the power, policies and rules provided a strict laws for companies. With the failure of big corporate houses like satyam in India which just not affected the foundation on Indian corporates but also resulted into big economic loss to our nation. Surely there arises a need to study those failure and creation of laws and strict rules. This paper is an attempt to analyses the problems with the corporates, effect of changing laws, analyzing the framework of companies. It covers the concept of corporate governance, its legal framework, its current status and how accounting may be practiced to protect corporate from corruption by establishing governance. It finds that better corporate frameworks benefit firms through greater access to financing, lower cost of capital, better firm performance, and more favourable treatment of all stakeholders.*

Keywords: *Corporate Governance, India, Scams, Stakeholder, Clause 49*

1. Introduction

: "Corporate governance" is a structure of conventions, protocols, proceedings, which distinctly defined the obligation and blameworthiness of different interest investors of corporate-houses. Enterprises amass backing from an enormous base both in the domestic and in the international capital markets. It is in this context, investment is ultimately an act of faith based on the ability of a corporation's management. When an investor invests money in a corporation, he expects the board and the management to act as trustees and ensure a minimum rate of return that is higher than the cost of capital. Corporate governance is 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.

The notion of ―corporate code of conduct‖ attribute towards companies' protocol account that detail principled ideals for their charge. A great deal of variation can be seen in the ways these statements are designed or outlined. These corporate codes of conduct are said to be comprehensively voluntary. They can acquire quite a few codec's along with target almost any difficulty viz. business office problems along with workers 'rights getting just one achievable type. Also, their setup would depend entirely within the company involved. In essence, both company governance as well as corporate ethics is necessary part for the profitable managing of an enterprise.

2. Corporate governance – theoretical framework

In order to confer about corporate governance we first authorize from the beginning who are the ones constituting and guiding the corporation. This function of the stakeholders is usually important when working with corporate governance, given that they have the

capacity to guide this company for the levels involving achievement or maybe the in contrast, to ―help‖ this are said to be unsuccessful. Of course, when talking about stakeholders with a major role into corporate governance, we agree that those are actually placed in the top part of the organizational structure of a company. William Pounds, former dean of MIT Sloan School of Management, in one of his lectures about corporate governance, approached an interesting way of explaining the way employees, management, executives, CEO and owners interact with each other (Figure no.1).

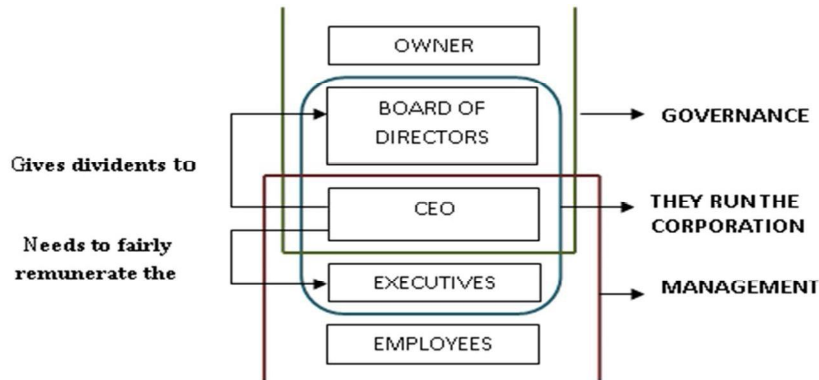

Figure 1: Company structure

(Source: Pounds, W. – William Pounds on Corporate Governance (speaker presentation), Carnegie Mellon Tepper School of Business)

It can be observed from figure no. 1, the CEO, after being selected by the board, is taking a considerable amount of obligation on his part in the company, having to decide on the remuneration for the executives and a decent chunk of dividends to board of directors. So CEO is indeed the one that maintains equilibrium in the structure trying to please everyone for the welfare of the organization.

Although corporate governance is often associated to executives of the organization, it could be seen throughout the paper, that there is a robust connection between corporate governance and ethics and/or social responsibility of the firm. Corporate governance emboldens a credible, principled, as well as virtuous environment. , the CEO, after being nominated by the board of directors, is taking a great burden in the company, the earnestness of the managers concerning the organization's fiscal outcomes and financial statements, the manager's way of handling the small stakeholders and many more.

Corporate governance is a phrase becoming more mundane today. In the past, businesses were handled and disciplined by the company owners but as firms have emerged and their needs heightened, this was no longer conceivable, the owner being contrived to gradually hand the power to managers. So, if corporate governance in early 50s was considered as bliss or utopia; but in recent antiquity it has become reality and

is said to be dominant concern. In the following figure the changes that take place in time within a organization can be seen, that William Pounds believes, is like a tectonic plate in continual motion and expansion.

Figure 2 Evolution of companies

(Source: Pounds, W. – William Pounds on Corporate Governance (speaker presentation), Carnegie Mellon Tepper School of Business).

However this peculiar scheme can be tested only in USA as other countries have contradictory ways of earmarking the authority in an organization. As it is often seen, all associations commence from the left side of the blueprint (even General Motors or IBM did), where the CEO is indeed the proprietor, but experience modifications along the way and the authority is given to other members, that have different interests in the business. Corporate governance is trying to reconcile, in the most efficient way possible, the desires and expectations of all stakeholders, in the corporate long-run welfare.

The consequence of corporate governance was realized back in the decade of 90's where a series of electrifying collapses of large private firms took place, actively stirring the belief of investors in the capability of the board in effective functioning of the organization. As a result of this scenario, Sir Adrian Cadbury in the year 1992, then head of the Committee on the Financial Aspects of Corporate Governance in the United Kingdom, issued The Cadbury Report in which he asserted over his worries related to corporate governance. Also in the report, he defined corporate governance as, arrangement by the means of which organizations are supervised and controlled‖. It means it can be seen as a set of structure through which corporate operate when proprietorship is segregated from management.

Through the times corporate governance has known by many definitions. One of which was advanced by the economists Andrei Shleifer and Robert Vishny in their paper review, which states that ―Corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment‖. It could be further expanded to explain corporate governance concerned with the settlement of concerted activity dilemmas among diffused investors and the rapprochement of difference of interest among various corporate stakeholders.

Organization for Economic Co-operation and Development (OECD) considers the role of corporate governance is to cite the promulgation of claims and loads among disparate categories of people engaged in the organization for e.g. like board of directors, various executives, shareholders and others, chartering rules and strategy plan for takings decisions for any organization. OECD considers corporate governance act as, both a set of association between management, shareholders and other stakeholders an arrangement through which organization outlines the objectives of an firm and required means to reach those, as well as it also act as system of incentives presented to the board and management in order to increase the objectives in the interests of shareholders and society.

But still why is corporate governance is such used term in our days and why firms are paying so much footage to it? The answers to why corporate governance is such used term come from many levels but necessarily it owes it emergence to the changes in the economy in past two decades. The private market based has become much more important today, for e.g. in the case of Romania where at the beginning of 90' most important sectors of the economy were owned by the state and when the communist regime collapsed, privatization played a crucial role in introduction of concept of corporate governance. Also due to technological advancement, liberalization and inaugural of financial markets ,structural reforms, and the allotment of funds among contending purposes which has become as such more and more complex, as has the following the use of that capital has become. This places good governance in much more pivotal role. And lastly the mobilization of funds, owing to the increased size of firms and crucial and expanding role of intermediaries. The owners today tend to sell their holdings in the public market and throw away their control, but also share the risk of the business with other investors which has raise the requirement of good governance much more firm strategies.

To acknowledge the second part focus our attention needs to be on the perks that corporate governance brings. Organizations who choose to embrace and comply to the corporate governance doctrine, enjoy a multitude of interests addressed such as the chance to avail capital at lower cost, attracting top talent for the firm, greater competitiveness, improved financial performance and more transparent workings, it has more favourable impact employment and compliance with good governance norms can the following beneficial to the owners and management of the organization.

- improved access to the capital and financial markets;
- helps in surviving in progressively competitive work environment through the means of mergers, acquisitions and by risk reduction through the ways of asset diversification;
- it provides an exit policy and ensures any clean inter-generational transport of money and also divestment of family members resources, along with lowering the chance pertaining to clashes of attention in order to crop up;
- a improved system of internal control, leading to increased accountability and improved profit margins;

- Possible future growth, diversification, or a sale, including the ability to attract equity investors – nationally and from abroad – as well as reduce the cost of loans/credit for corporations.

3. Models and principles of corporate governance

Corporate governance is being talked about internationally and as a result its almost everywhere that certain principles are being formulated or work about. Base of every principle lies in three leading principles since 1990 i.e. the Cadbury report (UK, 1992) , the principles of corporate governance OECD (1998 and 2004) , the Sarbanes oxley act (2002).

The major principles are listed below:

- Ensuring the basis for an effective corporate governance framework; the corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement author.
- The rights of shareholders and key ownership functions. The corporate governance framework should protect and facilitate the exercise of shareholders' rights.
- The role of stakeholders in corporate governance: The corporate governance frame work should recognize the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.
- The equitable treatment of shareholders: The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights.
- Disclosure and transparency: The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and governance of the company.
- The responsibilities of the board: The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders.

Corporate governance model around the world

There are many models operating in different countries depending on the capitalism in which they are made. The Anglo American model is one such model that rouse interest of many stakeholders. Main distinction lies between market oriented and network oriented models of governance. All the focus of every model is transparency yet they are distinct in every country they operate.

I. Continental Europe: some of the continental Europe including Germany and nether land, follows two – tire board of corporate governance. The board comprising of executive and supervisory and due to delegation of power differently it is considered to work more effectively

and efficiently. Flow at any point of time can be easily located in such model.

II. India: all power to create any rules in India lies with SEBI. According to SEBI stakeholders are primary responsibility of any company so any policy so framed must be made with due importance on stakeholders and their rights, as they are the ones who run the company.

III. United states, United Kingdom: these countries rely on Anglo American model, which is single tier model. It simply means that board of director have all responsibility and if anything goes wrong they are held responsible. Board usually comprise of executive and non-executive directors, where non-executive are more in numbers as compare to executives. Further non executives have to appoint an independent director, a separate audit committee and all such precautions as to make company works smoothly.

4. Mechanism of corporate governance in India

The Satyam Scandal

Satyam computer service was a publicly traded firm which has been detailed on the Bombay Stock market (BSE) and also the Nation's Stock market (NSE) with Indian, along with cross-listed on the Big apple Stock market (NYSE) in the USA. Although Satyam's promoters, represented by means of Mr. Ramalinga Raju along with his or her family, presented 8 percent from the gives inside firm at the end connected with '08, the corporation acquired a majority unbiased board as Independent composed of a number of Native Indian personages. Identified as some sort of "gold-plated collection" Satyam's self-sufficient administrators integrated some from Harvard business School mentor, the actual then-dean Indian Business School associated with Company along with an ex-Indian display case admin.

In the early part of the year 2009, Satyam experienced a pair of associated scandals, the primary a great aborted related-party purchase concerning the company's promoters, second one the actual exposing associated with heavy scams from the company's personal assertions. The Maytas purchase. On 16th December, 2008, Satyam's board convened a meeting to take into account the actual offered acquisition regarding Maytas Infra Limited and also Maytas Attributes Limited, firms centered on real estate and infrastructure improvement. Two major concerns they had to face were Firstly, the Maytas was concentrated on infrastructure development and real estate – both of which were the industries unknown and unrelated to Satyam's information technology as its own core activity. Secondly Raju's family owned approximately 30 of the ownership shares in Maytas Concern. It affected, the related-party transaction —would possess ended in a significant amount of cash flowing by Satyam to be able to it is personal causes, the actual Raju's family.‖ Even though several of Satyam's unbiased administrators questioned the actual offered transaction, the board of directors sooner or later acquired an answer to be able to continue using the offered buy. Satyam notified the board approval to the stock exchange which was needed beneath itemizing arrangement.

The market responded horribly to the announcement, leading to business swiftly withdrawing the actual Maytas pitch. On 7th of January 2009, shortly after the fall of Maytas transaction, Raju conceded about falsifying the financial

books of the organization, including some of the balance sheet errors showing exhibiting fictitious assets of over 1 Billion US Dollars. His confession further exposed that the prospective Maytas acquisitions was just false transactions which intended to wield the balance sheet statement of Satyam thereby wiping out the inconsistencies therein. Because of this data, Satyam's investment price slipped a different 60 to 70 percent, fundamentally obliterating the success and money of the Satyam investors. The particular aftermath, because of this scandal, this MCA, Government of India and SEBI investigations were bought upon. Raju who was the Satyam's managing director and company's CFO was arrested within days of his confession. Further two partners of Lovelock & Lewis, which was an Indian affiliate of Price Waterhouse Coopers and Satyam's auditor, were arrested further, and appointed all the new directors to replace the existing ones to continue the management of the company. Under the new administration and initiative, the company was able to take impressive turnabout. In the month of April 2009, Satyam was purchased by Tech Mahindra through the process of global bidding.

The worries raised by the cause of Satyam scandal echoed in corporate India much more broadly. In the recent study, the evidence of mass resignations by the independent director's post Satyam scandal with about 620 resigning in the year 2009 alone

A series of steps were taken by the initiative of Government and SEBI with the help of big corporate houses after scam to developed a more strict regime for the corporate in order to prevent economy from suffering badly and from sudden closure of industries and also to protect the interest of individual investors. Below is a timeline of various steps taken in India most important initiative is so far is taken up by SEBI by introducing clause 49 and in order to prevent fraud companies are required to follow it , details of clause 49 are given below:

Clause 49: Details

The main components of Clause 49 are summarized below:

Board of Directors: Independent

1. Requirement — 50 percent independent directors if Chairman is an executive director or 33 percent if Chairman is a non-executive.
2. Definition — no material pecuniary relationship or transactions with the company, its promoters, its management or its subsidiaries, not related to Board or one level below Board and no prior relationship with the Company for the last three years.
3. Nominee Directors of Financial Institutions — considered independent.

Board Requirements & Limitations

• Meet four times a year (maximum three months between meetings).

• Director may be on at most 10 committees and chair of at most five.

• Code of Conduct (Ethics) required.

Audit Committee:

Composition

• At least three directors (two-thirds must be independent).

• All members must be "financially literate" and at least one of them must

have "accounting or related financial management expertise."

• Chairman of the committee should be an independent director, who should be present at Annual General Meeting to answer shareholder queries.

Audit Committee Role & Powers

• Minimum of four meetings per year (gap between meetings not exceed four months).

• Broad role — review statutory and internal auditors as well as internal audit function, oversee a company's financial reporting process and quality of disclosure of financial information, and review whistleblower program if one exists, among other things.

• Powers to:

(i) investigate any activity within its terms of reference;

(ii) seek information from any employee;

(iii) obtain outside legal or other professional advice; and

(iv) secure attendance of outsiders with relevant expertise, if necessary.

Disclosures:

• Related party transactions.

• Accounting treatments and departures.

• Risk management.

• Annual report includes a detailed chapter on MD&A, including a discussion on industry structure and developments, opportunities and threats, segment-wise or product wise performance, outlook, risks and concerns, internal control systems and their adequacy, relating financial performance with operational performance, and issues relating to human resource development.

• Proceeds from offerings.

• Compensation for directors (including non-executives) and obtain shareholders' approval.

• Details of compliance history for last three years.

• Corporate governance reports (and discloses adoption, if any, of mandatory and non-mandatory requirements). Noncompliance with any mandatory recommendation with their reasons should be specifically highlighted.

• For appointment or re-appointment of a director, shareholders must be provided with the following information:

(i) a brief resume of the director;

(ii) nature of his expertise in specific functional areas; and

(iii) Companies in which he holds directorships.

• Information like quarterly results, presentation made by companies to analysts, etc., should be put on the company's web-site and sent in such a form so as to enable the stock exchange on which the company is listed to put on its own web-site.

Certifications:

• CEO & CFO: financial statements; effectiveness of internal controls; legal transactions; and inform audit committee of any significant changes in the above.

• Auditor or Company Secretary certifies compliance with corporate governance.

Other Recommendations: • Whistle blower policy is optional.

• Independent directors lose status as —independent‖ if they served nine years at company.

• Training board members.

• Evaluate non-executive board performance.

5. Key finding of frauds in India & Necessary Required Changes

Frauds have never stopped in fact after strict administration and laws. Keep factors that lead to scam even today are

- ❖ Diversion / theft of goods and money
- ❖ Bribery and corruption
- ❖ Regulatory non-compliance
- ❖ Fraud by senior management and conflict of interest
- ❖ Data or information theft

Many Indian companies operate in a family-owned culture. As a result of which it is often presumed that directors and manger know there job very well as they are the ones who r going to get most affected by it. Top brands like Aditya Birla group, reliance industries are the well know s examples of such groups where the profit of director is priority. Importance arise is to differentiate the key role of manger and directors separately. From a governance standpoint, boards should address the following key areas specifically concerning independent directors:

- ❖ Adoption of a formal and transparent process for director appointments. The conflict of interest involved in managements appointing independent directors should be tackled through nomination committees (comprising independent directors) for identification of directorial candidates
- ❖ Alignment of needs of the company to the skills required in the boardroom.
- ❖ Segregation of the roles of CEO and chairman of the board of directors.
- ❖ Planning for CEO and board succession in different scenarios.
- ❖ Formal evaluation of the CEO and senior management team's performance at least annually.
- ❖ Peer evaluation of independent directors should be adopted. This would enable independent directors to openly discuss amongst their group how they are performing and take tangible steps to improve their individual and collective functioning.
- ❖ Independent directors should take steps to make themselves aware of their rights, responsibilities and liabilities.

Protection for shareholders

Shareholder activism in India is at a nascent stage and comes to the force only in instances where institutional investors holding a significant stake are in a position to question the quality of corporate governance. As minority shareholders may not have complete understanding of their rights or the avenues through which these rights could be exercised, increased activism from institutional shareholders and reinforcing the role of independent directors on the board is likely to take shape in the near future. In the context of meeting expectations of stakeholders beyond the minority shareholders (e.g. employees, customers, vendors etc.) a number of initiatives need to be embraced such as:

- Informative Management Discussions and Analysis disclosures that focus on improving level of detail around operations and key risks
- Openness and transparency in dialogue with shareholders
- Objective and transparent whistle blower policies that are available to key stakeholders (employees, customers and vendors) and provide adequate safeguards against victimization of whistle blowers.
- Have minority shareholders' representatives on boards as independent directors.

Audit committee restructuring

Companies should address the challenges that their audit committees face and focus on enhancing skills in some of the most important areas listed below:

- Better understanding of risk, strategy and business models
- Understanding implications of the external environment on financial forecasts and performance
- Comprehend complex accounting policies and practices – how their application impacts results
- Monitoring fraud risk especially relating to senior management override of internal controls
- Assessing IFRS readiness and transition plans
- Monitoring ―tone at the top‖ in difficult times
- Effective oversight of internal and external auditors
- Ensuring that the board's strategic direction is in the best interest of all including minority shareholders
- Evaluation of audit committee and its members based on an established framework for its functioning.

For being the best organization which is being acknowledged at every level here arises the need for having an effective organization structure. This can only be possible after making some necessary changes and alterations. These changes are just not required at senior, top layer or only for the executives of the company. But our analysis says fraud occurs because there exist problems with decision makers. Hence a proper feedback and redressal mechanism is important to be incorporated in every organization by following a proper code of governance in order to build an integrated system of trust, transparency and accountability in every organization.

Conclusion

Failure is one such thing that happens due to internal weaknesses and flaws in management of the organization. Every company is following their own internal management system, hence there arise a need that they must adhere to strict rules and regulations as notified by government from time to time.

Since the late 1990s, significant efforts have been taken by Indian regulators, as well as by Indian industry representatives and companies, to overhaul Indian corporate governance. Government has taken many crucial steps to stop frauds but there is requirement of cooperation from companies to adhere to norms laid down. As possible ways to avoid future cases of collapse may be the following:

- Separation of powers of the Chairman and CEO. Each has to activate on its own pathway, otherwise we could reach a situation of excessive concentration of power and control capabilities of the supervisory board to be diluted.
- Integrity and missing of conflict of interest between managers, that should not target capital gains from the position they occupy, rather than wage remuneration they deserve.
- The existence of a strict flow of information so that decision-makers, have to receive timely and adequate information to perform their duties.
- Drawing concrete tasks and functions, especially in management teams, where decisions require a sustained effort and a great responsibility

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