



Corporate Governance in India

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ABSTRACT

The question of corporate governance in India has come mainly in the wake of economic liberalization, deregulation of industry and business as also the demand for new corporate ethos and stricter compliance with the legislation. The new economic policy adopted by the government of India since 1991 has necessitated the demand for introduction and implementation of a proper corporate governance policy in management of companies, not only in the interests of their stakeholders but also for the development of the economy. This paper intends to present the history of the evolution of corporate governance reforms in India and also highlights some of the challenges as well as measures to corporate governance in India.

KEYWORDS

Corporate governance, Evolution of corporate governance, Challenges and Measures.

INTRODUCTION -

Fine corporate governance has always been an issue since companies started using stock market to meet their financing needs. The history of East India Company suggest how the first publicly listed company's indulgence in trade and accounting malpractices led to the widespread public protests and demand for the reform. Executive greed, rampant corruption, insider trading and appalling corporate governance practices were all there. In India, every segment attached to the corporate has unanimously accepted the proposition that there is a need for practicing the corporate governance principles. India has a very long history of commercial activity and has always been a major source of many of the world's most sought after products. It is, therefore, governance practices in vogue at different points in time may be studied under three groups viz.

- 1 - The Managing Agency System (1850-1955)
- 2 - The Promoter System (1956-1991)
- 3 - The Anglo-American System (1992 and onwards).

REFORM PROCESSES -

The first reform came along with the English Companies (Consolidated) Act, 1908. The government decided to introduce a new Companies Bill in 1913 with the intention of addressing the issue of managing agents. However, it was only with the companies (Amendment) Act, 1936 that the Managing Agency System was actually acknowledged in company law and the problems related to it were addressed. Despite all these restrictions, Companies Act suffered a setback due to its failure to address many vital issues. A new Companies Act came into effect on 1st April 1956. This new Act contained 52 provisions restricting the activities of the managing agent.

In the Promoter System the Government was under great pressure to address the issues of corporate governance. It took many steps to promote responsible business practices. The Government introduced the Companies Act, 1956 to safeguard the shareholders' rights and placed stricter limit on the activities of the promoters. The Government also introduced a range of economic policies. Besides, the Government also provided for enforcement mechanisms, e.g. the Company Law Board, the MRTPC etc. Congress Government undertook a New Economic Policy in mid 1980s. The Government turned to the IMF for a loan in 1991. The conditionality of the IMF loan required a serious structural adjustment of the Indian economy, of which economic liberalization was an integral part.

The process of liberalization and globalization opened new

and exciting opportunities. The winds of liberalization blowing through the country had irreversibly changed the course of the business of the Indian corporate both in domestic and international market. The changes initiated during the last decade in terms of deregulations, simplification and harmonization of laws and procedures and the changes proposed to be effected in the Companies Act have clearly indicated the shift in government attitude to allow the corporate for self-regulation of their affairs. The changing business environment and activities have necessitated the need for reinstating the principles of corporate governance and professionalization of corporate management. The program of economic liberalization implied the need for change in the entire range of economic policy issues. The most significant with regard to our concern with corporate governance and emergence of an Anglo-American System are company law and the capital market.

HISTORICAL BACKGROUND -

After India got Independence in 1947, there were stock markets, a fairly developed banking sector and some British derived corporate practices for the corporations. Till 1991, the Indian government adopted socialist policies when government nationalized 19 banks and became the main provider of both equity and debt capital for individual firms. Capital provided to private firms by the government agencies were examined on the basis of the amount of funds invested rather than their returns on investment. Foreign competitions were repressed. Providers of debt and equity capital faced various hurdles due to long delays in judicial proceedings. Offering of public equity could be made only at the prices set by the government. Public companies in India were only required to comply with limited governance and disclosure standards enumerated in the Companies Act of 1956, the Listing Agreement, and the accounting standards set forth by the Institute of Chartered Accountants of India (ICAI). The process of Liberalization, Privatization, and Globalization started in 1991 and the Indian government introduced a series of reforms. With the abolition of the office of the Controller of Capital Issues, the Security and Exchange Board of India was constituted. It was established originally in 1988 but was only given statutory power the enactment of the SEBI Act in January 1992. SEBI formulated various rules and regulations for the purpose of regulating the operations of the players of the capital market, which were aimed at promotion of more responsible corporate governance. The need for capital led to corporate governance reform and many major corporate governance initiatives were launched in India since mid-1990s; most of these initiatives were focused on improving the governance climate in corporate India.

RECENT DEVELOPMENTS -

In India, the history of corporate governance got real momentum from the year 1998 and onwards, when the Confederation of Indian Industry (CII) framed a voluntary code of corporate governance for listed companies, named as CII of Desirable Corporate Governance. Consequently, the second major corporate governance initiative in the country was undertaken by SEBI. In early 1999, it set up a committee under Kumar Mangalam Birla to promote and raise the standard of fine corporate governance. Birla committee recommended-

- Board to set up qualified and independent audit committee to enhance credibility of financial disclosures and to promote transparency.
- Shareholders to exhibit greater degree of interest and involvement in the appointment of directors and auditors etc.

In order to hasten the process of bringing improvement in the companies functioning the government amended the Companies Act in 2000. The Amendment Act of 2000, increased manifolds the duties and responsibilities of the directors in the companies to improve corporate governance. Immediately after the provisions of the Companies (Amendment) Act 2000 came into force, SEBI in its meeting held on 25th January 2000, decided to make amendments to the Listing Agreement by inserting a new Clause 49. The new Clause 49 dealt with corporate governance and included the aspects

- Appointment of optimum number of executive, non-executive/independent.
- Appointment of audit committee.
- Remuneration of directors and its disclosure.
- Board procedure and meeting.
- Report on corporate governance.
- Management report.

Consequently, the Government of India promptly appointed the Naresh Committee in 2002 to examine and recommend drastic amendments to the law pertaining to auditor-client relationships and the role of the independent directors.

The fourth initiative on corporate governance in India is in the form of the recommendations of the Narayana Murthy Committee. This Committee was set up by SEBI under the chairmanship of N.R. Narayana Murthy, chairman and mentor of Infosys, in order to review Clause 49 and to suggest measures to improve corporate governance standards. The Committee recommendations included independent directors, audit committees, audit reports, directorship and director compensation, codes of conduct, financial disclosures, related party transactions and risk management. Murthy Committee examined a range of corporate governance issues relating to audit committees and corporate boards and disclosure of shareholders. In its present form, Clause 49, called "Corporate Governance", contains eight sections dealing with the Boards of Directors, Audit Committee, Remuneration of Directors, Board Procedure, Management, Shareholders; Report on Corporate Governance, and Compliance, respectively. Firms that do not comply with Clause 49 can be de-listed and charged with financial penalties. Corporate governance reforms efforts in India did not stop after adopting the Clause 49.

The Government constituted an Expert Committee on Company Law under the Chairmanship of Dr. J.J. Irani on 2 December, 2004. Irani Committee recommended the Government of India to introduce the Company Bill 2008 in the Indian Parliament. This Bill aimed that the corporate sector in India should

operate in regulatory environment. The Companies Bill, 2008 was lapsed due to the dissolution of the 14th Lok Sabha but the government decided to re-introduce this Bill as the Companies Bill, 2009 without any change in it except the Bill year because of its suitability for issues related to corporate governance. At the end of 2008, India experienced a massive corporate governance scandal involving Satyam Computer Services (Satyam), one of India's largest information technology companies. Indian government took quick actions against this scandal. This necessitated a re-assessment of the country's progress in corporate governance. As a result, the CII began examining the corporate governance issues. The National Association of Software and Services Companies (NASSCOM) also formed a Corporate Governance and Ethics Committee chaired by N.R. Narayana Murthy. Additionally the Institute of Company Secretaries of India (ICSI) has also put forth a series of corporate governance recommendations.

The revised Bill, namely, the Companies Bill, 2011 was introduced in the Lok Sabha on 14th December, 2011; however the same was withdrawn by the Government on 22nd December and sent back for consideration by the Standing Committee on Finance. The Companies Bill 2012, passed by Lok Sabha on 18 December, 2012, includes a number of new provisions aimed at improving the governance of public companies. Indian market regulator, the SEBI, recently issued a consultative paper on review of corporate governance encouraging a wider debate on governance.

CHALLENGES OF CORPORATE GOVERNANCE IN INDIA -

There are some practices prevalent in the market which is posing challenges to corporate governance in our country.

- Lack of financial transparency.
- Weak and non-transparent monitoring system.
- Monopoly of family firms.
- Low respect for shareholders.
- Unsophisticated equity market vulnerable to manipulation.
- Corruption level becomes visible only after a revelation of big financial scam.

MEASURES FOR EFFECTIVE CORPORATE GOVERNANCE -

For effective corporate governance, there is an earnest need to follow some measures-

- The evaluation of performance of board members should be independent and transparent.
- All the members of organization must know, understand and respect the codes of conduct.
- The auditing system should be proper and transparent in order to check financial irregularities and frauds.
- Accurate information regarding developments, threats and risks related to financial and economic matters in annual reports and on the company websites.
- Ethical behavior of corporation or of any member at board or management level should be rewarded.

CONCLUSION -

At present, corporate governance reforms in India are at a crossroads; while corporate governance codes have been drafted with a deep understanding of the governance standards around the world, there is still a need to focus on developing more appropriate solutions that would evolve from within and therefore address the India-specific challenges more efficiently.

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