CORPORATE GOVERNANCE - IS IT A LEGAL ISSUES IN INDIA

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Abstract

*The burgeoning economic growth that corporate India witnessed since the 1990s brought to the forefront the need for Indian companies to adopt corporate governance practices and standards, which are consistent with international principles. Industry groups, notably the Confederation of Indian Industries ("**CII**"), spearheaded the move to bring corporate governance issues to the attention of Indian companies and also led to the introduction of legislative reforms prescribing the manner in which Indian companies could implement effective corporate governance mechanisms. Corporate governance is perhaps one of the most important differentiators of a business that has impact on the profitability, growth and even sustainability of business. It is a multi-level and multi-tiered process that is distilled from an organization's culture, its policies, values and ethics, especially of the people running the business and the way it deals with various stakeholders. In this paper attempt has been made to elaborate the Corporate Governance needs, Prerequisites and constituents. It also discuss about corporate governance guidelines lay down the rules to be followed by all stakeholders. It also discuss the legal issues of corporate governance in India.*

***Keywords**: Corporate governance, stakeholders, committees, boards.*

Introduction

Virtuous and upright corporate governance practices are a sine qua non for viable business. It marks for creating long-term significance to all its shareholders and other stakeholders. Regulators such as the Ministry of Corporate Affairs and SEBI govern and administer some facets of corporate governance that is protected in the law. A transparent, ethical and responsible corporate governance framework is very much needed for good governance. These generally radiate from the fundamental will and appetite that is embedded in the business entity. It is the global financial crisis during the recent past and corporate failures etc. that have accelerated the adoption of basics of corporate governance that help in building trust and increasing confidence among the stakeholders. The introduction of corporate governance strengthens reputation and goodwill, develops an image built on reliability, accountability and transparency.

Prerequisites and Constituents of Corporate Governance

Today assumption of good Corporate Governance practices has evolved as an essential component for conducting business. It is not only a pre-requisite for facing strong competition for viable growth in the emergent global market situation but is also an personification of the considerations of fairness, accountability, disclosures and transparency to boost significance for the stakeholders.

Studies of corporate governance practices across several countries conducted by the Asian Development Bank, International Monetary Fund, Organization for Economic Cooperation and Development and the World Bank reveal that there is no single model of good corporate governance.

Range of different approaches to corporate governance have been developed which are recognized by the OECD Code that acknowledges different legal systems, institutional frameworks and traditions across countries. However, a high degree of importance has been assigned to the shareholders interest who place their trust in corporations to use their investment funds wisely and effectively which is mutually followed by all good corporate governance administrations.

In the light of the underlying principles of corporate governance, business knowledge resource online mentions three basic inter-related segments, which are

- Integrity and Fairness
- Transparency and Disclosures
- Accountability and Responsibility

These segments lay down the premise for the Board of Directors, the Shareholders and the Management whose job is to ensure that there exists

1. A clear, explicit, understandable and unmistakable jurisdictive and regulatory framework for effective corporate governance.
2. It is important that the codes of conduct of an organization are communicated to all stakeholders.
3. The objective of the company must be clearly documented in a long-term corporate strategy.
4. There should be a clearly established process of identifying, analyzing and treating risks, which could prevent the company from effectively achieving its objectives.
5. An independent board is essential for sound corporate governance. It means that the board is

capable of assessing the performance of managers with an objective perspective.

6. Board appointments ensure that the most competent people are appointed in the board and all the board positions must be filled following all rules.
7. It is essential to ensure that directors remain abreast of all development, which are or may impact corporate governance and other related issues.
8. The board requires comprehensive, regular, reliable, timely, correct, and relevant information in a form and of a quality that is appropriate to discharge its function of monitoring corporate performance.

Administrative and Legal Machinery of Corporate Governance in India

Corporate governance is beyond the realm of law. It cannot be regulated by legislation alone. Legislation can only lay down a common framework – the "form" to ensure standards. The "substance" will ultimately determine the credibility and integrity of the process. Substance is inexorably linked to the mindset and ethical standards of management. However, the present structure works on the following parameters:

- It is the Indian Companies Act 1956, the Securities and Exchange Board of India (SEBI) and the professional body of auditors created by the Institute of Chartered Accountants of India (ICAI) which are the legal and institutional mechanisms in India to oversee and control the financial reporting by Indian companies.
- In India there is no specific corporate governance code for all companies. Clause 49 of the Listing Agreement for listed companies and voluntary guidelines for corporate governance issued by MCA are the codes followed.
- The structure of the board is unitary and as per Indian Companies Act, 1956, a private company must have a minimum of two directors whereas a public company must have at least three directors. There is no limit on the maximum number of directors.
- The law states that in case of number of independent directors of a listed company, at least 50% of the total number of directors must be non- executive directors. Further, if the chairman of a company is a non-executive director, at least one-third of the total number of the company's directors must be non-executive. On the other hand, if the chairman is an executive director, then at least one-half of the total members should be independent directors.
- Further regarding tenure of office of directors, In the case of public companies and private companies that are subsidiaries of public companies, one-third of the total number of directors are permanent directors and two-thirds of the directors are rotational directors. One-third of the rotational directors must retire by rotation at every annual general meeting. The term of any director required to retire by rotation cannot exceed three years and this term can be extended by re-appointment only. A director retiring by rotation can be re- appointed at the same annual general meeting.
- As regards frequency of Board Meetings, a minimum of 4 Board meetings must be held in each year. There should not be a time gap of more than 4 months between any 2 Board meetings. However, the Audit Committee must meet at least 4 times a year –once in every 4 months and once before the finalization of accounts. The quorum for the meetings of the Audit Committee will be 2 or one-third of the total number of members; whichever is higher At least 2 of the members constituting a quorum must be independent.
- There is no such provision for separation of positions of chairman and CEO. The same individual may perform both the roles.
- An audit committee is to be formed which shall have a minimum of 3 members, all being non-executive directors, majority of the members being independent. At least 1 member must have financial and accounting knowledge. The chairman, being an independent director, shall remain present at the company's AGM to respond to the shareholders' queries.
- Clause 49 of the Listing Agreement imposes a non mandatory requirement on listed companies to have a whistle blowing policy. A company may establish a mechanism for employees to report to the management concerns about unethical behavior, actual or suspected fraud or violation of the company's code of conduct or ethics policy. This mechanism could also provide adequate safeguards against victimization of employees who use the mechanism and direct access to the chairman of the audit committee in exceptional cases. There is no other statute in force, which provides statutory protection for whistleblowers.
- Lastly, listed companies must comply with the mandatory provisions set out in Clause 49 of the Listing Agreement. The annual report of a listed company comprises the company's financial

statements, the directors' report and such other disclosures as are required under Clause 49 of the Listing Agreement. In relation to unlisted public companies and private companies, the directors must disclose in the directors' report all the pertinent information.

One of the most noteworthy progress in the stream of corporate governance and investor protection was the formation of the securities market regulator, the Securities and Exchange Board of India in 1992. The Confederation of Indian Industry (CII) released a Desirable Code for Corporate Governance in 1998 followed by the codes of two sequential committees instituted by SEBI. The instant result was the origination of Clause 49 of the Listing Agreement which is the most meaningful and momentous development in Indian legal regime linking to corporate governance. This clause, announced in 2000 and revised later, specifies the standards of corporate governance that is a prerequisite for every listed company to be adopted and followed. Clause 49 of the listing agreement recommends numerous corporate governance means in the following subject areas:

- Board of Directors and Independent Directors
- Audit Committees
- Subsidiary Companies
- Disclosures
- Report on Corporate Governance
- Compliance Certifications

Similarly, the Government of India, through Ministry of Corporate Affairs (MCA) took many initiatives to boost the corporate governance framework in India. Some such measures are as follows:

- Voluntary Guidelines on Corporate Governance released in 2009
- Green Initiatives
- Serious Fraud Investigation Office ("SFIO")
- Investor Grievances Management Cell ("IGMC")
- National Foundation for Corporate Governance ("NFCG")
- Recently Companies Act 2013 has been enacted which is a step towards replacing the six decades old and outdated company legislation. The new Act has numerous procedures to strengthen the legal structure of corporate governance such as class action suits, whistleblower policy, corporate social responsibility, prohibition of insider trading, entrenchment provisions among others. However, it is too early to comment upon the implementation and working of these new measures.

Conclusion

Corporate Governance is beyond the realm of Law. It stems from the culture and mindset of management and cannot be regulated by legislation alone. Corporate Governance is all about openness, integrity and accountability. It is a key element in improving the economic efficiency of the firm. Credibility offered by Corporate Governance also helps in improving the confidence of the investors – both domestic and foreign. It involves a set of relationships between a company's management, its Board, shareholders and Stakeholders.

The Code of Business Conduct and Ethics helps ensuring compliance with legal requirements and other standards of Business Conduct. All company Employees and Trainees are expected to read and understand this code of ethics, comply with all applicable policies and procedures, and ensure that all agents and contractors are aware of, understand and adhere to these standards. The Company expects all employees, agents and contractors to exercise good judgment to ensure all employees, agents and contractors and to maintain competitive, efficient, positive harmonious and productive Work Environment and business organization.

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