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Corporate Governance in India: Structure and Practice Analysis

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Abstract

Purpose **-** Corporate governance is about encouraging openness, accountability and corporate disclosure. The corporate governance framework defines the assignment of rights and obligations among various corporate members such as executive boards, directors, shareholders and other parties concerned and describes corporate decision-making rules and procedures. By doing this, it offers the framework by which the goals of the organisation are set along with the means to achieve these goals as well as to track results. Corporate governance practises apply to the laws for the effective management of companies. This document includes a detailed analysis of the Indian corporate governance system and practises. The paper starts with a presentation of India's corporate management history and explores the journey for almost two decades.

Design/methodology/ approach- The diagnostic study analyses corporate governance structure and practices in detail through major regulatory changes, regulatory review mechanism(s), established standards and initiatives taken by various core committees, groups and related bodies. It further evaluates if, and to what extent, good governance is translating into value to various stakeholders of the company. The paper attempts to identify gaps and outline the scope for improvement.

Findings - There is an extensive effort to strengthen the processes of corporate governance in India, but it is evident that governance improves over time due to implemented policies and the general growth of the economy. The activities of an organisation change as it adapts to evolving circumstances.

Originality/value – This study provides a survey of the structure and practices of corporate governance in India since its inception.

Keywords*- Corporate governance, India*

Introduction

With the unpleasant experiences of corporate scandals and deficiencies arising from human failures in financial, administrative and audit oversight, the issue of corporate governance has taken on a sharper emphasis. Corporate governance is about encouraging openness, accountability and corporate disclosure. The corporate governance structure defines the assignment of rights and responsibilities to various corporate members such as executive boards, directors, shareholders and other parties concerned and describes corporate decision-making rules and procedures. Through doing so it provides the context within which the organization's priorities are set along with the means to achieve and control outcomes. Corporate governance practises apply to the laws for the effective management of companies. In India, corporate governance reforms started as a reaction to changes that took place worldwide after the Indian government targeted domestic economic liberalisation and globalisation.

The challenges of Indian corporate governance

The position of large shareholders, where the equity of a corporation is concentrated in the limited number of individuals and institutions, has been studied in a number of studies, in making management accountable as opposed to distributed shareholders and their effectiveness in the corporate governance of companies (Berle and Means, 1932, Shleifer and Vishny, 1997). A two-edged sword, with its own merits and demerits, is the involvement of major shareholders. Large shareholders are likely to be more successful than small and dispersed shareholders in controlling company management, on the one hand, since these investments are subject to significant assets and the necessary voting power (Berle and Means, 1932; Jensen and Meckling, 1976; Fama and Jensen, 1983; Shleifer and Vishny, 1986). Dodd and Warner (1983) conclude that the problem of collective action among scattered shareholders is likely to be resolved by large shareholders in the disciplining inefficient management. In the other hand, the disincentive of such large shares is the expropriation of minority shareholders and the conflict of interests between large shareholder interests and minorities (Fama and Jensen, 1983, Shleifer and Vishny, 1997). Another cost of concentrated ownership is that big shareholders cannot consider the risk of a reduced diversification (Demsetz and Lehn, 1985; Fama and Jensen, 1983). Some recent research has shown that excessive management monitoring can result in high levels of ownership. Reduction of the company-specific investments management initiative (Demsetz, 1997; Burkart, Gromb, and Panunzi, 1997).

The corporate governance literature identifies two problems: agency problem and the problem of minority shareholder protection. The Indian corporate structure is that of large shareholders which are generally the promoters (family owned business) and a widely dispersed minority and therefore, the main issue seems to protect minority or exploitation of minority shareholders by the promoters. These large business houses are often seen expatiating and drifting the funds among group companies. Indian markets are dominated by family companies. According to a 2010 report by Credit Suisse, the group comprises 663 of its 983 businesses. They control a business in an undue manner either directly through the promoter's family share or through a holding company. As a part of the nominal gross national product (GDP), India has expanded from 9% in 2001 to 46% in 2010, above the largest number of Asian economies in terms of the number of family businesses. In the hands of the firms' promoters and, to a lesser degree, the ownership of the India corporate sector remains based, pursuant to the Government of India, Ministry of Finance, Company Affairs, 46th Annual Functioning and Management Report, 1956. Among all listed companies in India, the average equity holdings are 48.1 percent of promoters, 8.7 percent of private corporate bodies, 9.3 percent of international investors, 4.5 percent of banks and FIs, 1.7 percent of mutual funds, 7.4 percent of government shares and 31.8 percent of the public. The cross-prevalence ownership holdings, together with strong ownership involvement, make India's corporate control structure similar to a "insider" one as described by Sarkar and Sarkar (1999).

What has changed since the SEBI was formed in 1992?

International capital is necessary as a temporary measure with the advent of the 1991 fiscal crisis, when domestic capital is insufficient for economic growth purposes and when the capital market is in the process of development One of the truth is that the need for capital has led to a corporate governance reform, and that since the middle of the 1990s many big corporate governance initiatives have been introduced in India. In 1992 the Securités and Exchange Board of India (SEBI), the regulator of India's securities market, was set up. The Confederation of Indian Industry (CII), the Indian Industry's first major corporate governance initiative, set up the first voluntary "Desirable Corporate Governance: A Code" in 1998 on the advice of MR Rahul Bajajaja' s National Working Group. The first voluntary initiative was the Indian Industry and Business Association. The code was voluntary, contained broad provisions and centred on the listed businesses. The second big corporate management programme has been undertaken in the country by SEBI. SEBI formed a committee in early1999 under Kumar Mangalam Birla to promote and enhance standards of good governance. The SEBI Board accepted and ratified in 2000 the Birla Committee's core recommendations that were included in the Stock Exchange Listing Agreement, Article 49, with a view to composing and compensating non-executive directors for disclosure of the board. The central government has set out the law (Compliance Certificate) for the companies 2001 to resolve divergent formats on mandatory corporate governance disclosures under the powers conferred by subsection (1) of section 642 of the Companies Act of 1956. It published formats and Secretarial Specifications by the Council of the Institute of Corporate Secretaries (ICSI).

By 2002, several forward-looking businesses had complied with the voluntary code issued by the CII and disclosed the extent to which they had complied with the code in their annual reports. Therefore, India has a basic corporate governance structure in place. Nevertheless, it was firmly felt that a statutory and not voluntary code would serve the basic function of Indian conditions.
Governance of businesses. The Department of Corporate Affairs (DCA) has set up a "Naresh Chandra Committee" (2002) under the Minister for Finance and Company Affairs to address a variety of corporate management issues. The committee primarily concentrated on the independent board and audit monitoring and on improvements in financial and non-financial disclosures. There have been some issues about substantive or formal compliance with discrepancies in the accuracy of annual reports, including transparency. SEBI considered that corporate governance should not be reduced to merely a ritual, with the SEBI set up a committee for the review of clause 49, under the leadership of Mr N. R. Narayana Murthy. The Committee recommended audit committees, audit reports, independent officers, related parties' transactions, risk management, compensation for directors and directors, ethical codes and financial records. SEBI directed every stock exchange, through a replacement of 'Revised Article 49' (2006), with 'Revised Clause 49' (2006), to amend the listing agreement by superseding current Article 49 with more thorough and comprehensive standards in terms of corporate governance, thus imposing additional duties on businesses to ensure that their homes are safe, transparent and accountable. ICSI has extensively updated and adjusted the formats for new clause 49 of the listing agreement.

The Ministry of Entrepreneurship formed another committee headed by M. J. Irani to put in best practise from all over the world to develop a well-regulated climate. MCA was also re-designed and updated the Corporate Act of 1956. The Companies Bill 2008 was drawn up on the advice of the Iranian Commission. After almost five years of debate, the plan was finally approved as the Companies Act in 2013. The Act of 2013 has introduced several new concepts and is all about a rule-based law. The key features are:

• One female manager at least

• At least one Indian Resident Manager

• Defined role and responsibilities by independent director (ID).

• ID database to maintain; you can select IDs from this database.

• Compared to two previously, the company was approved by one person

• Full Directors increased to 15; Special Resolution for all additional Managers

• Up to 20 directors per person; up to 10 public enterprises;

• Partnership Committee Introduced Stakeholders

• Compulsory recruitment of key management personnel (KMP)

• Directors responsible for identifying and operating internal financial controls •

• Strengthened sanctions for directors substantially

SEBI and MCA head the corporate governance system in India; SEBI with its listing agreement and MCA with the Company Rule. Legislations have the strongest governance system and procedures, but because of the prevailing judicial structure and corruption, their implementation is the biggest obstacle. With respect to 17 codes out of 19 required codes of the listing agreement, the compliance rate is greater than 80 percent.

What is the effect of the changes since the establishment of SEBI in 1992?

Balasubramanian, Black, Khanna (2008) found that the Indian Corporate Governance Index (ICGI) and firm market value are related to the major enterprises included on the BSE200 index in their 2006 Clause 49 report. It is meaningless for smaller companies. This is possibly attributed to multinational businesses with a high media profile, strong analyst coverage and large foreign shareholding. They also state que, while there is space for improvement, it is relatively strong for the responding companies to comply with Indian governance rules and that improved governance appears to be in line with a stronger market value for at least larger companies. In addition, the most close relations occur with the increase in firm market value among the elements of accountability governance and shareholder rights.

The state of business administration in India - A survey (2008) of the Institute of the Audit Committee confirms that principle-based principles with moderate regulations and robust regulatory review frameworks are better suited to improving corporate governance. A 'principle-based approach' usually means the circulation of a cogent collection of standards and preferred practises that businesses are asked to follow as they see fit with their unique circumstances.

Sanan, Yadav (2011) prepared for sample firms a pre-reformation (2001-02 to 2004-05) and post-reformative (20055-06 to 2008-09). The 30 Bombay Stock Exchange (BSE) listings are based on the Ordinary, Bad and Public (S&P) attributes of openness and disclosure survey (2008). The study shows that Indian businesses have only a limited degree of financial transparency in the midst of major changes in corporate management. It highlights the need for improved legal and regulatory system implementation to enhance financial reporting efficiency.

Conclusion

The reform of corporate governance systems and practises has been important, but the problem of corporate governance violations in India mainly linked to abuses by centred or large shareholders, can be tackled externally (Jayanth Rama Varma 1997). Corporate governance, at the same time goes beyond corporate law, making it very difficult to address the issue. It is not a matter of simply meeting the legal requirements, but of maintaining the board's dedication to operating the business in a consistent way to maximise the value of long-term shareholders.

There is a significant effort to improve corporate governance processes in India, while governance is clearly improving over time as a result of the implemented policies and overall economic growth. The activities of an organisation change as it adapts to evolving circumstances. The economic and industrial climate in which a company operates evolves as competition rises and technology progresses. The framework and practises of corporate governance will need to change in such a changing world and in the years to come, the present forms the basis. The changing principles are consistent with business complexity and strengthen the need for ethical governance, management and the need to look beyond basic processes and procedures. In reality and not only type the requirements for compliance. In terms of its corporate governance regulations, India contrasts favourably with most other developed and Asian economies from a purely regulatory point of view. The existing laws under clause 49 and the revised company law of 2013 refer to the core principles of good governance. However, strengthened corporate governance is regulated not only by enhanced law but also by a principle-based approach.

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