# CORPORATE GOVERNANCE IN INDIA – CHALLENGES AND SUGGESTIONS

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## ABSTRACT

Corporate governance is an amalgamation of rules, regulations, and by-laws through which the corporate entities are run, managed and controlled. The concept of corporate governance in India was prevailing from the 1960s but in terms of practical implementation, it still lags behind where India is witnessing various numbers of scams each year. This paper provides the meaning of the term corporate governance and also explains the significance of corporate governance. The paper makes an effort to identify the ways in which the principles of ethics can be balanced with the profit-making intentions of the companies. It also analyses the development and working of clause 49 of SEBI. The paper also explains the role of independent directors in the company's success. The Indian model of corporate governance is one of the best corporate governance models around the world yet we see a various number of scams happening due to flawed application of its principles and policies. For e.g. Indian model of corporate governance gives a priority to the recognition of shareholder's rights but in terms of implementation, it is seen that companies follow poor disclosure practices, lack of transparency, not prioritizing shareholder's interest leading to scams and manipulation of public money. The paper puts forth the challenges in the Indian model of corporate governance and provides suggestions that might be implemented to bring ethical and transparent corporate governance in the country. This paper examines the relationship between the Tata - Mistry controversy and corporate governance principles. This is a qualitative research paper dealing with the concept of corporate governance in India.

***Keywords*****:** Corporate governance, clause 49, independent directors, ethical principles, Tata –

Mistry.

## INTRODUCTION

Corporate governance is basically all about the governance system in a corporation to prevent scams and financial irregularities and promote corporate growth and success. In today's business world Corporate governance plays a crucial role to attract investors and improve the overall value of the enterprise. Corporate governance principles in India were followed from the early 1960s to attract foreign customers and foreign investments in the country but gained more prominence in the 1990s during the globalization era.

## MEANING OF CORPORATE GOVERNANCE

In simple terms, Corporate Governance is a system of governance that regulates corporations. Corporate governance is a set of rules and regulations that govern, operate, manage, and regulate corporate firms. Corporate governance works on balancing the interest of the company with that of the interest of its shareholders and stakeholders. Corporate governance contains a set of principles that a corporate firm should follow for profit gaining and corporate growth. In recent times strict adherence to Corporate governance principles is observed by many corporate entities for the entity's success.

## SIGNIFICANCE OF CORPORATE GOVERNANCE

When a company strictly adheres to corporate governance principles it increases accountability in the company which helps in the prevention of corruption and scams from occurring in the company. Through corporate governance, a company can effectively control the company's management by imposing certain principles that should be strictly followed by management such as transparency, accountability, and fairness. Corporate governance also helps the company to follow corporate social responsibility and helps in balancing the interests of the company and community. Corporate governance imposes a sense of responsibility on the BOD holding them responsible and accountable to shareholders and stakeholders of the company.

Through Corporate governance, the powers of directors are regulated to an extent preventing them from arbitrary use of their power. Corporate governance not only protects the interest of the company but also protects the interest of all those who have their interests in the business. Attracting foreign currency and foreign investments has becomes a priority in today's business world which can be certainly achieved by following corporate governance principles.

## OBJECTIVES

The main output of this study is:

- To identify the ways in which the principles of ethics can be balanced with the profit-making intentions of the companies.
- To analyse the development and working of clause 49 of SEBI.
- To understand the Tata – Mistry controversy in relation to corporate governance principles.
- To put forth the challenges and suggestions that might be implemented to bring ethical and transparent corporate governance.

## METHODOLOGY

The methodology adopted for research & the collection of data is through secondary sources. The collection of data through the secondary source involves the collection of information from the persons who have already conducted the study in the respective field. This is a doctrinal type of research where secondary sources such as books, articles, journals, research papers, library materials, statutes, international conventions, online sources, & other relevant subject matters are taken into consideration. The collection of information is done up to my knowledge & is concerned with the topic in question.

## WAYS TO BALANCE PRINCIPLES OF ETHICS AND PROFIT-MAKING INTENTIONS OF COMPANIES

Business ethics is an unseen force upon which the growth pillars of the business stand.

***The pillars of Corporate Governance***

- **Transparency:** A company must disclose all the required information about its financial and non-financial activities from time to time. In particular, the company must disclose all the major changes that occurred in finance along with profits and losses incurred in its annual financial statements or annual reports.
- **Fairness:** The company needs to be impartial and must provide just treatment to all the members of the company without any favoritism and bias. An environment with respect and equal treatment with open and honest communications must be present in the company.
- **Accountability:** Other than concentrating on profit-making for the shareholders, the management should also be held accountable and protect the shareholders' interests. The company should also prioritize the interest of its stakeholders and be accountable to them such as providing a safe working environment for the employees of the company and delivering quality products and services to its customers.
- **Integrity:** This results in effective decision-making in the company taking into account the interest of shareholders and stakeholders. Besides profit-making it also helps the company to sustain in the market for a long period of time.

***The Balance***

- **Transparency and Accountability** – when all the financial statements and decisions of the company are revealed to its shareholders it helps in gaining the shareholder's trust which results in capital gains and the overall financial growth of the company takes place.
- **Fairness** – when all employee in the company are treated equally and when their opinion is taken into consideration while decision-making it leads to the satisfaction of employees which in turn increase the work efficiency or overall performance of the

employees in the company will improve.

- **Integrity** – when the interest of the company and shareholders are one and the same it helps in the betterment of business ethnicity which at the end result in the overall growth of the company and attracts sustainable profits.

All these together result in good corporate governance which results in corporate success and economic growth.

## ROLE OF INDEPENDENT DIRECTORS IN IMPROVING THE CORPORATE GOVERNANCE PRACTISES IN THE COMPANY

Involvement of independent directors in the board is considered to be more efficient as there is a requirement to keep a check upon the executive directors of the company and to make sure that the top-level management is completely adhering to the law and are following the ethical standards that are required to maintain good corporate governance.

Complete independence to the top-level management leads to prejudicial interests and capricious decision makings which would benefit only the executive directors and affect the interest of all parties who have their interests in the business.

While executive directors concentrate on improving the company on financial grounds, the independent directors concentrate on the growth of the company upon the pillars of accountability, transparency, and ethics which are vital for good corporate governance. Companies with independent directors on the board are proven to have good corporate governance which in turn contributes to corporate success and economic growth.

As independent directors concentrate on maintaining the transparency between the company and the shareholders, they act as trustees of shareholders and safeguard their interests which in turn contributes to maintaining investor`s confidence which leads to the capital growth of the company which is again one of the benefits of having good corporate governance.


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## WORKING OF CLAUSE 49 OF SEBI GUIDELINES ON CORPORATE GOVERNANCE

Upon the suggestions of Narayana Murthy committee Clause 49 of The Listing Agreement was revised by SEBI as a step towards increasing the prominence of corporate governance in India. Due to various scams that took place in India, Clause 49 was forced to be reformed to avoid certain problems that affect the company and the country`s economy.

1. **The Disclosure Policy** - This policy under clause 49 has proven to be the most effective measure to fulfil the aim of Corporate governance as this policy under clause 49 helps in maintaining the transparency between the company and shareholders which in turn restore the trust and confidence of the company in the eyes of their shareholders. Disclosure and transparency are the fundamental characteristics of good Corporate governance which are consecutively attained by companies when they comply with Clause 49 (1).
2. **Composition and Responsibility of the Board** - The BOD play a crucial role in the company`s success as they put in their maximum efforts for bringing the company to distinctive heights. Separation of executive and non-executive role`s under clause 49 in the board helps in fortification of the overall integrity of the company. The inclusion of independent directors to the boards helps in effective monitoring and upholds better standards of corporate governance in the company. The accountability of the board under clause 49 is another facet that contributes to good corporate governance as it ensures efficiency, effectiveness, and transparency in the business carried by the directors of the company.

## TATA – MISTRY CONTROVERSY AND CORPORATE GOVERNANCE

***The Background***

- **2006** - A year after his father`s retirement from the Tata Sons, Cyrus Mistry joined the board.
- **2013** - Mistry became the chairman of Tata Sons.
- **2016** - Board members voted for the removal of Mistry as chairman of Tata Sons.

***The Legal Controversy (Forum – Decision - Reasons Stated)***

**NCLT** - Justified the removal of Mistry from Chairmanship - Mismanagement, worked only for gaining power over the company, non-adherence to law.

**NCLAT** - Reinstatement of Mistry as Chairman - The removal was illegal, reinstatement of new chairmen was oppressive, there was no due process followed, conversion of a public company into a private company is unlawful.

**Supreme Court** - Stay on NCLAT order - Presence of lacunae in the order, granted relief which was not prayed (contentions by Mistry was on wrongful removal not on reinstatement).

***Controversy and Corporate Governance***

The principles of Corporate governance were clearly violated by both the parties in the given controversy.

**Company** - The Company did not give prior notice to Mistry concerning his removal from the Chairmanship. There was a lack of transparency and accountability between the company and its shareholder (Mistry).

**Shareholder (Mistry)** - Lack of leadership skills (clash of culture between old guards of Tata and new people), non-adherence to the law (dispute between DoCoMo and Tata), mismanagement of Tata Sons (sales of Tata assets in order to pay back the debt)

**Overall Integrity** - When the objectives and interests of the company and shareholders are undivided and complete it results in the overall growth of the company. But in this controversy, there was a conflict of interest between the company and Mistry which implies the violation of Corporate governance in the company.

## CHALLENGES AND SUGGESTIONS

1. **Separate legal entity:** The identity of members of the company is merged with the identity of the company. The members of the company who involve in corrupt practices or scams continue such acts because the identity of the company is merged with the identity of its members. It should not be ignored that a company is a separate legal entity

and has its own separate identity from its members. With the help of lifting of the corporate veil, the number of scams and manipulations happening in the company can be prevented by holding the individuals responsible and accountable for the wrong done.

2. **Conflict of interest:** When there are different interests between the company and its members it always results in poor management of the company which in turn results in the downfall of the company's growth and success. Internal governance plays a major role in deciding the company's growth and downfall. If the internal conduct in the company is effectively and efficiently functioning such as the board of directors making decisions that are best for the company's shareholders and stakeholders rather than solely concentrating on the profit making, this results in the overall company's growth and success. The values and views of shareholders should always be taken into account and the company should always be accountable to shareholders to gain their trust upon the company. Corporate integrity should be followed within the company to overcome this challenge because when the interests of stakeholders and shareholders are complete and undivided it results in a positive impact in the society, employee satisfaction, longevity, better company culture which altogether result in corporate success.

3. **Independent directors:** Independent directors who play an important role in the company's success are easily removed from the company without serving any prior notice about the removal. Independence should be given to the directors to make decisions that are best for the company. The power which vests in the promoters should be limited by giving independence to the directors to take effective decisions that are profitable for the company.

4. **Adherence to law**: on one hand India has a solid framework of Corporate governance laws but on the other it has poor implementation of such laws. Most of the companies in order to gain the best financial results tend to do unethical or illegal activities. Strict adherence to the laws along with following the ethical standards results in good corporate governance.

5. **Composition of the board**: Companies with the right proportion of executive and independent directors are proven to be effective. But in certain companies, it is seen that the position of the board of directors is occupied by the founder's family members

without taking into account whether such persons are capable or qualified to manage the company or not.

6. **Accountability to stakeholders**: Companies often concentrate on being accountable to shareholders alone to attract investments and increase capital gain but accountability to stakeholders is one such aspect that is often neglected by the companies. The company should be held accountable to the stakeholders and the company should interact with its stakeholders and take into consideration their concerns during the decision-making process in the company.

7. **Recognition/Appreciation**: when employees are often appreciated for the work done, it develops a sense of commitment towards their work and the company. Giving incentives and bonuses to the employees results in employee satisfaction which attracts loyalty towards the company which results in overall productivity.

8. **Risk management**: when certain corporate policies undergo failures, an effective risk management committee with the right contingent plans for the unforeseen circumstances makes a company stand out from the rest of its competitors.

9. **Code of conduct**: A rigid code of conduct holds no good in the long run. The code should be feasible and flexible in order to meet the needs. The code of conduct should be formulated in such a way that it is easy for the directors and the employees in the company to follow.

10. **Penalizing**: There is a need for rigid penal provisions for wrongdoers for the non-compliance in order to reduce the scams from occurring. A Strict penalty should be imposed when the company does not adhere to the law or not comply with the corporate governance principles.


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