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M.Sc (Maths), M.B.A. (Mktg.), M.B.A. (H.R.),
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Cell No. : 9579260877, 9822620877, Ph.No. : (0240) 2400877

E-mail : ajanta1977@gmail.com, www.ajantaprakashan.com

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17. Corporate Governance - Development in India

Dr. Ashok R. Shinde
H.O.D. of Commerce, Y.C. College Islampur, Dist. Sangli, B.O.S. Member , Shivaji University, Kolhapur.

Abstract

Corporate Governance is integral to the existence of the company. Corporate Governance is needed to create corporate culture of transparency, accountability and disclosure refer to compliance with all moral & ethical values, legal framework & voluntary adopted practices. This enhances customer satisfaction, shareholder value and wealth.

Introduction

Over the past two decades, the investment world has seen large number of scandals, which creates instability and insecurity among the investors as well as stakeholders of the company. It is failure of governance. It is social responsibility of corporate body to act in a manner, which is compliance with law, SEBI guideline and sustainable development . Corporate Governance means to steer an organisation in desired direction. The responsibility to steer lies with the board of directors governing board. Therefore a company must have an effective ethics programme to ensure that all employees understand its value and comply with the policies and codes of conduct that create ethical climate. Company should create two types of control system one is compliance oriented programme and other one is values oriented programme. Under first one control system, employee comes to know legal terms, statues and contracts as well as rules and penalties for non-compliance. Second one control system emphasis on to develop shared values, the focus is more on an abstract core of ideas such as respect and responsibility company's values are seen as something to which people willingly aspire.

Objective of Study

1. To understand the concept of corporate Governance.
2. To study the development of corporate Governance in India.
3. To study the various recommendation given by various committee.
4. Corporate Governance impact on social environment.

Research Methodology

The present study depends upon secondary data which has been collected through books, journals, articles, internet etc.

Corporate Governance

Meaning

The root of the word Governance is from 'gubernate' which means to steer. Corporate or corporation is derived from latin term 'corpus' which means a body. Combined Corporate Governance means a set of system procedures, policies, practices, standards put in place by a corporate to that relationship with various stakeholders is maintained in transparent and honest manner.

Definition of Corporate Governance by Various Committee

1. **Report of N.R.Narayana Murthy committee on Corporate Governance constituted by SEBI (2003)**

Corporate Governance is the acceptance by management of the inalienable rights of shareholders as the true owners of the corporations and of their own role as trustees on behalf of shareholders. It is about commitment to values, about making distinction between personal & corporate fund in the management of a company.

2. **Report of Kumar Mangalam Birla Committee constituted by SEBI (1999)**

Strong Corporate Governance is indispenable to resilient and vibrant capital markets and is an important instrument of investors protection. It is the blood that fills the veins of transparent corporate disclosure and high quality accounting practices, It is muscle that moves a viable and accessible financial reporting structure.

3. **Confederation of Indian Industry (CII) (1998)**

Corporate Governance deals with laws procedures practices and implicit rules that determine a company's ability to take informed managerial decision vis-a-vis its claimants – in particular, its shareholders, creditors, customers, the state and employees. There is a global consensus about the objective of good corporate governance maximising long term shareholder value.

Development of Corporate Governance in India

Evidence of Corporate Governance from 'Arthashastra'

Kautilya's Arthashastra maintain that for good governance all administrators including the king were considered servants of the people Good governance and stability were completely linked. If rules are responsive, accountable, removable, recallable, then there is stability, if not then there is instability. These rules hold good even today.

The substitution of the state with the corporation the king with CEO or the board of a corporation, and the subject with the shareholders, bring out the quintessence of corporate governance is the belief that public good should be ahead of private good and that the corporation's resources cannot be used for personal benefit. Kautilya's fourfold duty of king –

1. Raksha - literally means protection equated with the risk management aspect.
2. Vriddhi- literally means growth in the present day context can be equated to stakeholder value enhancement.
3. Palana- literally means maintainance/ compliance. It can be equated to compliance to the law in letter and spirit.
4. Yogakshema- literally means well being and in kautilya;s Arthashastra, it is used in context of a social security system it can be equated to corporate social responsibility.

Arthashastra talks self-discipline for a king and the six enemies which a king should overcome – lust, anger, greed, conceit, arrogane & foolhardiness. In the present day context, this addresses the ethics aspect of businesses and the personal ethics of the corporate leaders. Corporate Governance pillars on transparency and fairness in action satisfying accountability and responsibility towards the stakeholders.

Role of Law in Corporate Governance

Law can only provide a minimum code of conduct for proper regulation of human being or company. Law is made not to stop any act but to ensure that if you do that act, you will face such consequences that are 'good for good' and 'bad for bad' thus in same manner, role of law in Corporate Governance is to supplement & not to supplant. It cannot be only way to govern Corporate Governance but instead it provides a minimum code of conduct for good corporate governance, Law provides certain ethics to govern one and all so as to have maximum satisfaction and minimum friction. It plays a complementary role. Role of law in Corporate Governance is in companies Act which imposes certain restriction on directors so that there is no misrepresentation of document, there is no excessive power so that it imposes duty not to make secret profit and duty to act in the best interest of the company etc.

Corporate Governance in Companies act – 2013

The following are the important provisions under the Companies Act 2013

Section – 149 to 151

This section talks about minimum & maximum number of Directors, independent directors, woman director & small shareholder's director. This section provides criteria to appoint director

Section – 134

This section states Directors Responsibility Statement and additional disclosure in the report of the Board of Directors.

Section – 166

Duties of the directors are given in this section.

Following notes are provided in Act in accordance with above mentioned section

a) Qualification of directors
b) Remuneration to directors
c) Terms or tenure of director
d) Code for independent director
e) Rules, functions and duties of directors
f) Manner of appointment & reappointment
g) Resignation or removal of directors
h) Board meeting and its time interval in a year
i) Audit committee, meeting of audit committee power & role of Audit committee
j) Nomination & Remuneration committee
k) Risk Management
l) Related party Transaction
m) CEO & CFO certification
n) Report on Corporate Governance
o) Serious fraud investigation office

National Committees on Corporate Governance (1998)

A] Confederation of Indian Industry

For the first time in the history of Corporate Governance in India, the confederation of Indian Industry (CII) framed a voluntary code of Corporate Governance for the listed companies, which is known as CII code of desirable Corporate Governance

The main recommendations of the code are summarised below

1. Any listed company with a turnover of Rs.1000 million and above should have professionally competent and acclaimed non executive directors.
2. For the non executive directors to play an important role in corporate decision making and maximum long term shareholder value.
3. Directors need to become active participants in board, not passive advisors, director should well known about responsibilities within the board.
4. Director should know how to read a balance sheet, profit & loss account, cash flow statement and financial ratios and have some knowledge of various company law.
5. No single person should hold directorship in more than 10 listed companies. It is very much required to justify the role of directorship.

6. Board should meet a minimum of six times in a year, at an interval of two months.
7. Various key information must be reported to and placed before the board that is annual budgets, quarterly results, internal audit reports, show cause, demand and prosecution notices received fatal accidents and pollution problem, default in payment of principle and interest to the creditors, inter corporate deposits, joint venture foreign exchange exposure.
8. Listed companies (whose shares are quoted on a stock exchange) whose turnover of over Rs.1000 million or paid up capital of Rs. 200 million should set up Audit Committee –
    i. The committee should consist of at least three members
    ii. Who should have adequate knowledge of finance, accounts and basic element of company law.
    iii. The committee should provide effective supervision of the financial reporting process.
    iv. The audit committees should periodically interact with statutory auditors and internal auditors to ascertain the quality and authenticity of the company's accounts as well as the capability of the auditors themselves.

B] Kumar Mangalam Birla Committee (2002)

Another committee named as K.M.Birla committee was set up by SEBI in the year 2000 In fact this committee introduced clause – 49 Listing Agreement to be compiled with by all listed companies. Practically most of the recommendations were accepted and included by SEBI in its new clause 49 of listing agreement in 2000 The main recommendation of the committee are –

1. The board of company should have an optimum combination of executive and non-executive directors. The ratio should be equal of executive & non-executive directors.
2. Independent directors are directors who do not have any financial relationship or transaction with the company apart from receiving directors remuneration.
3. A director should not be a member in more than ten committees across all companies in which he is a director.
4. The disclosure should be made in the section on Corporate Governance of the annual report, regarding remuneration packages of all directors, details of fixed component and performance linked incentives along with the performance criteria, service contract, notice and period severance fees, stock option details, if any.

5. In case of appointment of a new director the shareholder must be provided information regarding a brief resume of the director nature of his experience in specific functional areas and names of companies in which the persons hold directorship.
6. Board meeting should be held at least four times in a year with maximum gap of 4 months
7. A qualified and independent audit committee should be set up by the board of the company in order to enhance the credibility of the financial disclosure of a company and promote transparency.
8. The board should set up a remuneration committee to determine on their behalf of the shareholders with agreed terms of referee the company policy on specific remuneration package for executive directors including pension rights and any compensation payment.
9. A board committee under the chairmanship of non-executive director should be formed to specifically look into the redressal of shareholder of balance sheet, declared dividend etc.
10. The companies should be required to give consolidated accounts in respect of all their subsidiaries in which they hold 51% or more share capital.
11. Management should disclose to the board relating to all material, financial and commercial transaction where they have personal interest that may have a potential conflict with interest of the company at large.
12. Management discussion and analysis report should form part of the annual report to the shareholder.
13. The company should arrange to obtain a certificate from the company's auditor regarding compliance of mandatory recommendation and annex the certificate with director's report.

C] Reserve Bank of India, Report of the Advisory Group on Corporate Governance (2001)

An advisory group on Corporate Governance under the chairmanship of Dr. R. H. Patil then, Managing director of National Stock Exchange was constituted by standing committee of RBI in 2000. They submitted their report, in March 2001. Recommendation given by this committee is very much similar to above mention committee report.

D] Naresh Chandra Committee (2002)

Government of India appointed Naresh Chandra Committee in 2002 to examine and recommended drastic amendments to the law pertaining to auditor-client relationship and the role of independent director

The main recommendations of the committee are given below –

1. The minimum board size of all listed companies as well as unlisted public limited companies with paid up share capital & free reserve of Rs.100 million & above or turnover of Rs. 500 million and above should be seven of which at least four should be independent directors.
2. As per international best practices, the committee recommended a list of disqualification for audit assignment which included prohibition of
   a) Any direct financial interest in the audit client.
   b) Receiving any loans and guarantees.
   c) Any business relationship
   d) personal relationship by the audit firm, its partners as well as their direct relatives.
   e) Undue dependence on an audit client.
3. Certain services should not be provided by an audit firm to any audit clients that is –

a) Accounting and book keeping
b) Internal audit
c) Financial information design
d) Actuarial
e) Broker. dealer, investment advisor, investment banking
f) Outsourcing, valuation, staff recruitment for the client etc.

4. There should be a certification on compliance of various aspects regarding Corporate Governance by the CEO and CFO of a listed company. It is interesting to note that majority of the recommendation of this committee are the culmination of the provision of Sarbanes Oxley Act of the USA

E] N. R. Narayana Murthy Committee (2003)

SEBI constituted this committee under the chairmanship of N. R. Narayana Murthy, chairman and mentor of Infosys and requested the committee to review the performance of Corporate Governance in India and make appropriate recommendation. The committee submitted its report in February 2003 The main items of committee recommendations are as follows.

1. Person should be eligible for the office of non-executive director so long as the term of office did not exceed nine year.
2. The age limit for directors to retire should be decided by companies themselves.
3. All audit committee members shall be non-executive directors. They should be financially literate and at least one member should have accounting related financial management expertise.
4. Audit committee of listed companies shall review mandatorily the information.
   a) Financial statement and draft audit report.
   b) Risk management report.
   c) Management discussion and analysis of financial condition and operating results.
   d) Statutory auditors letter to management regarding internal control weakness and related party transaction.
5. The audit committee of the parent company shall also review the financial statement in particular the investment made by the subsidiary company.
6. Companies raising money through an Initial Public Offering (IPO) shall disclose to the audit committee the uses/application of funds by major category on a quarterly basis. On an annual basis the company shall prepare a statement of funds utilised for purpose other than those stated in the offer document/prospectus. This statement shall be certified by the independent auditors of the company The audit committee should make appropriate recommendations to the board to take up steps in this matter.

Conclusion

Corporate Governance is the system of rules practices and process by which a firm is directed and controlled here we can conclude that –

1. Responsibility of Governing Company in a right manner lies on the shoulders of the board of directors, auditors and audit committee.
2. SEBI is established by aiming to protect the interest of investors in securities and to promote the development of and to regular the securities market in the purview of law.
3. Principles of Corporate Governance are transparency and accountability in transactions and reporting authentic information to stakeholders.
4. Evidence of Corporate Governance traced from Kautilya's Arthshastra in this also king is just care taker of nation. Its role is similar to board.
5. One more concept highlighted here is Corporate Social Responsibility. It is forward stage of Corporate Governance. Wealth maximisation of shareholder is more important than merely profit maximisation of company.

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