



CORPORATE GOVERNANCE IN INDIA: A STUDY OF THE NEED, RELEVANCE AND SIGNIFICANCE FROM A MACRO PERSPECTIVE

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Abstract

Corporate Governance (CG) scenario in India has undergone radical changes during the last two decades notwithstanding the fact that as a whole India's position in this regard is still in its infancy. A number of commendable initiatives, including regulatory measures, have been implemented by the Government of India or various statutory bodies. The implementation of the new Companies Act 2013 has given another impetus to the CG scenario in India. These reforms have had positive but gradual impact on the corporate governance practices in Indian corporates including the state-owned public sector enterprises (PSEs). In spite of these positive trends, it may be pointed out that corporate governance in India has to traverse a long way to catch up with the global best practices in this regard. For instance, it was in the recent past that India's corporate world experienced a number of mis-governance and scams. In this context, this paper analyses the need, relevance and significance of CG in India; based on the recent developments like the mandatory CG provisions as envisaged under the new Companies Act 2013.

Key Words: *Corporate Governance (CG), Public Sector Enterprises (PSEs), Mandatory CG.*

1.INTRODUCTION

India has become one of the fastest emerging nations to have aligned itself with the international trends in Corporate Governance (CG). As a result, Indian companies have increasingly been able to access to newer and larger markets around the world; as well as able to acquire more businesses. The response of the Government and regulators has also been admirably quick to meet the challenges of corporate delinquency. As the global environment changes continuously, there is a greater need of adopting and sustaining good CG for value creation and building corporations of the future. It is true that the CG has no unique structure or design and is largely considered ambiguous. There is still lack of awareness about its various issues, like, quality and frequency of financial and managerial disclosure, compliance with the code of best practice, roles and responsibilities of Board of Directors (BOD), shareholders rights, etc. There have been many instances of failure and scams in the corporate sector, like collusion between companies and their accounting firms, presence of weak or ineffective internal audits, lack of required skills by managers, lack of proper disclosures, non-compliance with standards, etc. As a result, both management and auditors have come under greater scrutiny. But, with the integration of Indian economy with global markets, industrialists and corporates in the country are being increasingly asked to adopt better and transparent corporate practices. The degree to which corporations observe basic principles of good CG is an increasingly important factor for taking key investment decisions. If companies are to reap the full benefits of the global capital market, capture efficiency gains, benefit by economies of scale and attract long term capital, adoption of corporate governance standards must be credible, consistent, coherent and inspiring.

Quality of CG primarily depends on following six factors, viz. (i) Integrity of the management; (ii) Ability of the Board; (iii) Adequacy of the processes; (iv) Commitment level of individual Board members; (v) Quality of corporate reporting; and (vi) Participation of stakeholders in the management; etc.

2. RELEVANCE AND SIGNIFICANCE OF THE STUDY

Since this is an important element affecting the long-term financial health of companies, good governance framework also calls for effective legal and institutional environment, business ethics and awareness of the environmental and societal interests. After understanding the need for good CG, it becomes necessary to understand what it means by good governance. Regulators, courts and investors frequently extol the virtues of

'Good Corporate Governance' (or, 'Good CG', in short) in organisations but often fail to define exactly what that means. It's often a case of "we'll know it when we see it" or, in the case of the regulators, courts and investors, "we know what it isn't when we see it". It is important to understand that what would be considered 'Good CG' and also how it differs for each individual organisation according to its circumstances. What is inadequate for one organisation may be onerous for another. It is also important to realise that good corporate governance isn't just about compliance. Whilst CG will keep one out of trouble, it would not help his organisation to be successful.

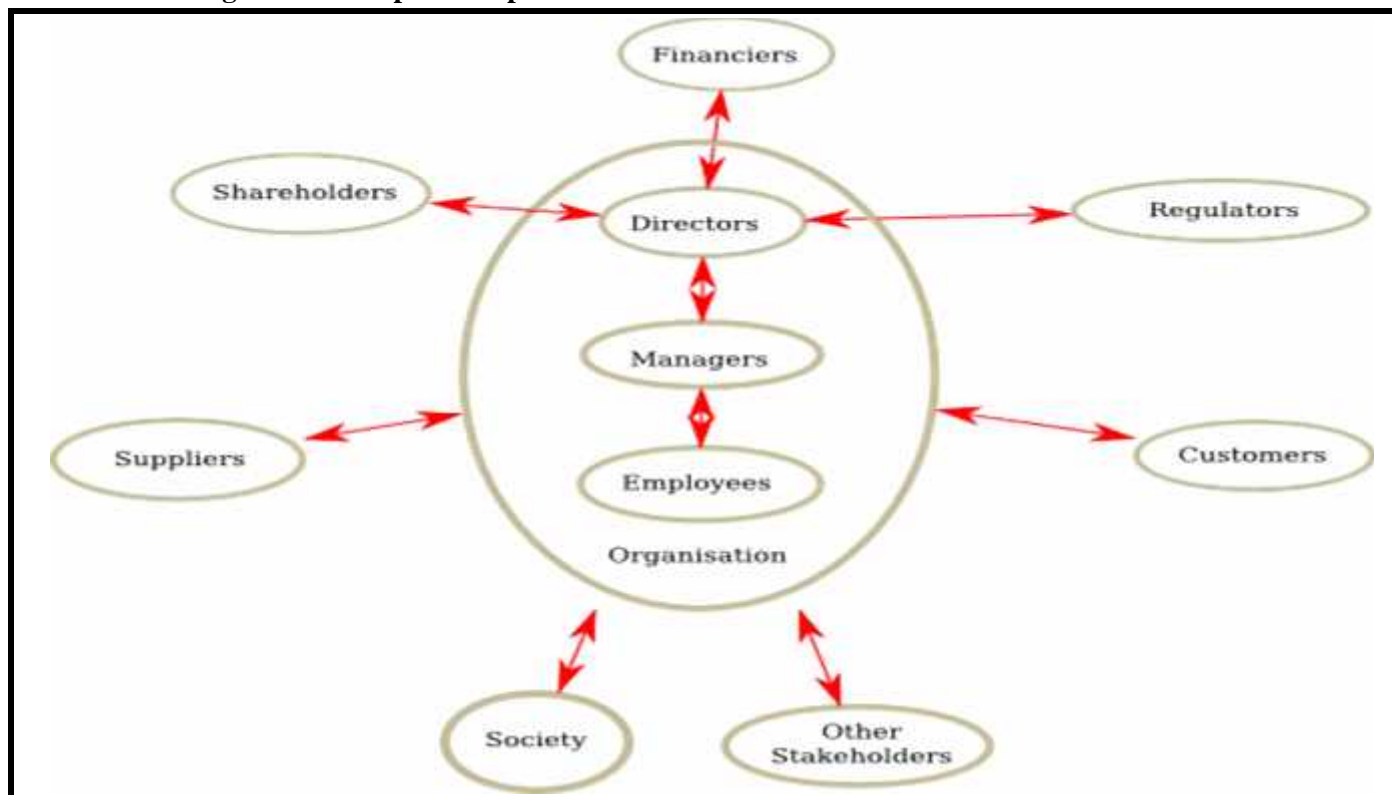
3.OBJECTIVES OF THE STUDY

1. To examine the current discourses on 'Corporate Governance' (CG) and to understand what constitutes 'Good Corporate Governance' (Good CG) from a fundamental level;
2. To assess the need, relevance and significance of CG in India from a macro perspective in view of the recent developments like the mandatory CG provisions;
3. To suggest suitable strategies for more effective adoption of CG in India for the purpose of enhanced performance of organisations.

4.CONCEPT OF CORPORATE GOVERNANCE (CG)

To understand the concept of CG, its interactions with various stakeholders in the environment needs to be studied. (Figure I). As shown CG have vast relationships with multiple stakeholders.

Figure I: Concept of Corporate Governance and its interaction with various stakeholders



The most fundamental definition for CG is based on the idea that an organisation is essentially a nexus of contractual agreements between many parties for the purpose of achieving the organization's objectives. These parties include shareholders, directors, managers, suppliers, employees, customers, financiers, government authorities, other stakeholders and the society in which the company operates. Whilst some of these contractual agreements are formal written ones, many are implicit. Likewise, some of these contractual agreements are financially based but many are not. (Figure I). Although the company enjoys the status of a person through legal fiction, in reality a company is constituted entirely by the actions and interactions of people with other people,

products of technology, systems, and the natural world. CG involves managing the framework within which these complex relationships operate.

The quality and nature of these relationships has a strong influence on the long term financial interests of the organisation. It can be expected that the negotiation and administration of these contractual agreements to the benefit of each of the parties involved will maximise the long term results of the organisations. So good CG is all about ensuring that the needs and interests of all of an organisation's stakeholders are taken into account in a balanced and transparent manner. However, good CG is not just a matter of having the right policies and procedures in place. It has to be embedded into the culture of the organisation from the very top down. Systems and structures can provide an environment conducive to good CG practices, but at the end of the day it is the acts or omissions of the people charged with relevant responsibilities that will determine whether governance objectives are in fact achieved.

Good CG is also no guarantee of success. It is a necessary but not sufficient foundation for success as strategic factors play a more important role in determining the eventual success or failure of an organisation. In the majority of large business failures, it is essentially the failure of the underlying business strategy that causes each business to fail. CG issues allow the flawed businesses to continue and amplify the magnitude of their eventual collapse. Now when we have a clear picture of the meaning of Good CG, it is worth understanding about the regulatory bodies in India, who formulate, implement and monitor the guidelines on corporate governance. In India, SEBI (Securities and Exchange Board of India), MCA (Ministry of Corporate Affairs) and DPE (Department of Public Enterprises) are the main governing bodies.

5. EMERGENCE OF THE CONCEPT OF MANDATORY CG PROVISIONS

It was in June 2007 that the Government of India (GOI) introduced the guidelines on CG for CPSEs on a voluntary basis. As such, these guidelines on CG were not mandatory in India till 2012. Thereafter, the governance scenario in the country was affected by the 'negative' nature of India outlook as signified by the 'BBB-' grading allotted to it in respect of Long-term Sovereign Rating, by M/s. Standard & Poor, the Credit Rating agency. This negative credit rating for the country issued in April 2012 highlighted the weakened credit profile of India. Because of these ratings the country was losing on investments and the economy went dipping down. Taking stock of this account, the regulatory bodies formulated the new Companies Act 2013 and made implementation of Corporate Governance, mandatory.

From the Public Sector perspective, the Department of Public Enterprises (DPE) under the Government of India (GOI) took a serious note of implementing and monitoring corporate governance (CG) in the PSUs. As per the statistical data made available by the DPE, GOI in its report as of FY 2014 (Table I), nearly 50 percent of the total CPSEs in India had 'Excellent' rating in the CG front, while over one-fourth of them have only 'Poor' grade. The rest about one-fourth have either 'Very Good' or 'Good' grades. [GOI, DPE (2014)]. (Table I).

Table I: Grading of CPSEs on the basis of their compliance with CG Guidelines

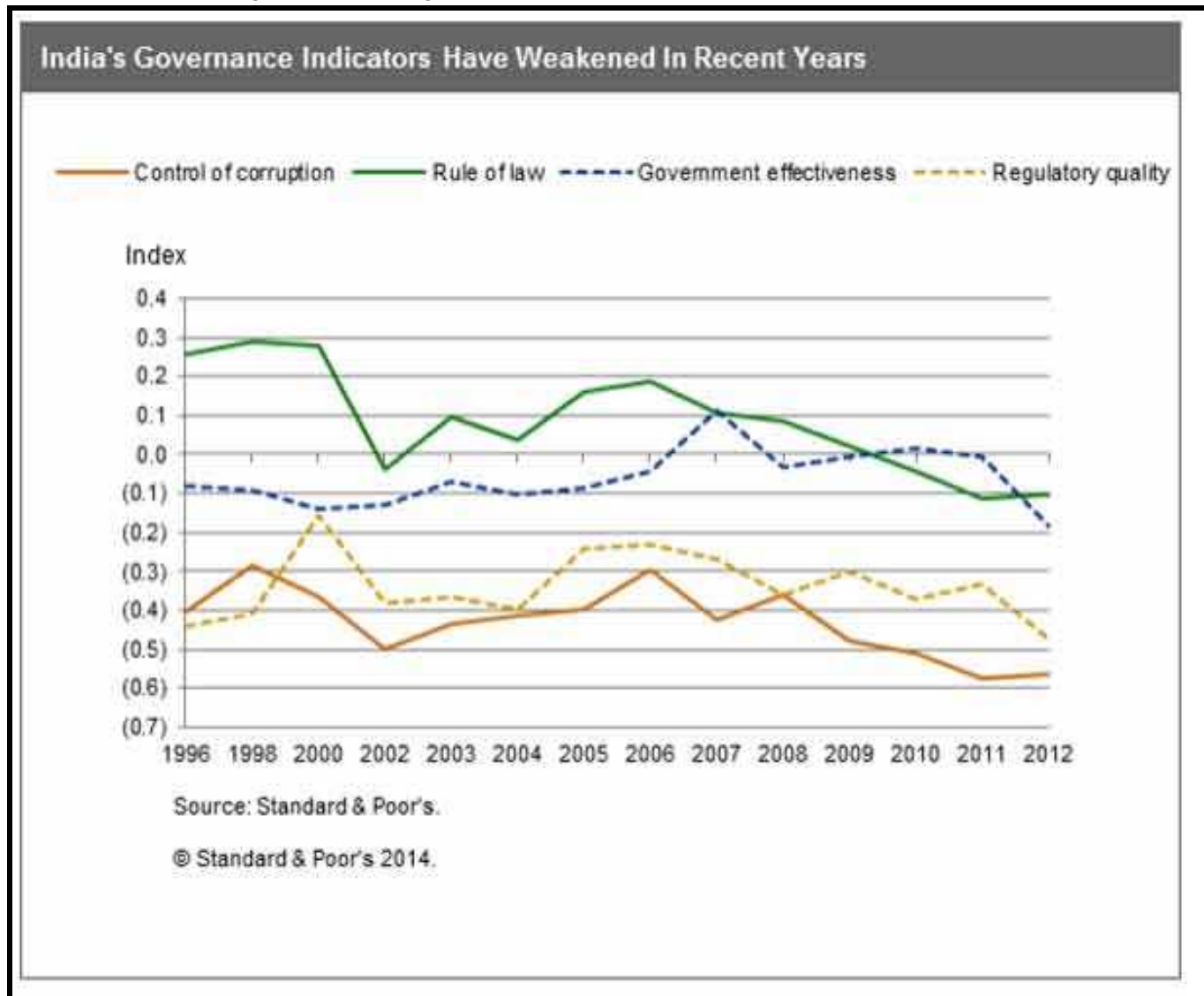
F.Y	Excellent	Very Good	Good	Fair	Poor	Not Complied	Not Applicable	Under Liquidation	Not started Operations	Exempted	Total
2012	78	34	28	11	12	80	1	2	2	--	248
2013	112	26	14	8	81	--	19	--	--	--	260
2014	135	28	24	3	69	--	--	1	--	17	277

Source: Govt. of India, Dept. of Public Enterprises (DPE) (2014).

6. IMPLICATIONS OF MANDATORY CG PROVISIONS ON THE GOVERNANCE SCENARIO IN INDIA

As already noted the declining trend in various governance parameters of India till 2012 leading to negative credit rating for the country has prompted the country to go for mandatory CG provisions and accordingly such mandatory clauses were included in the new Companies Act 2013. The dwindling pattern of governance parameter(s) till 2012 (Figure II) could be reversed since 2013.

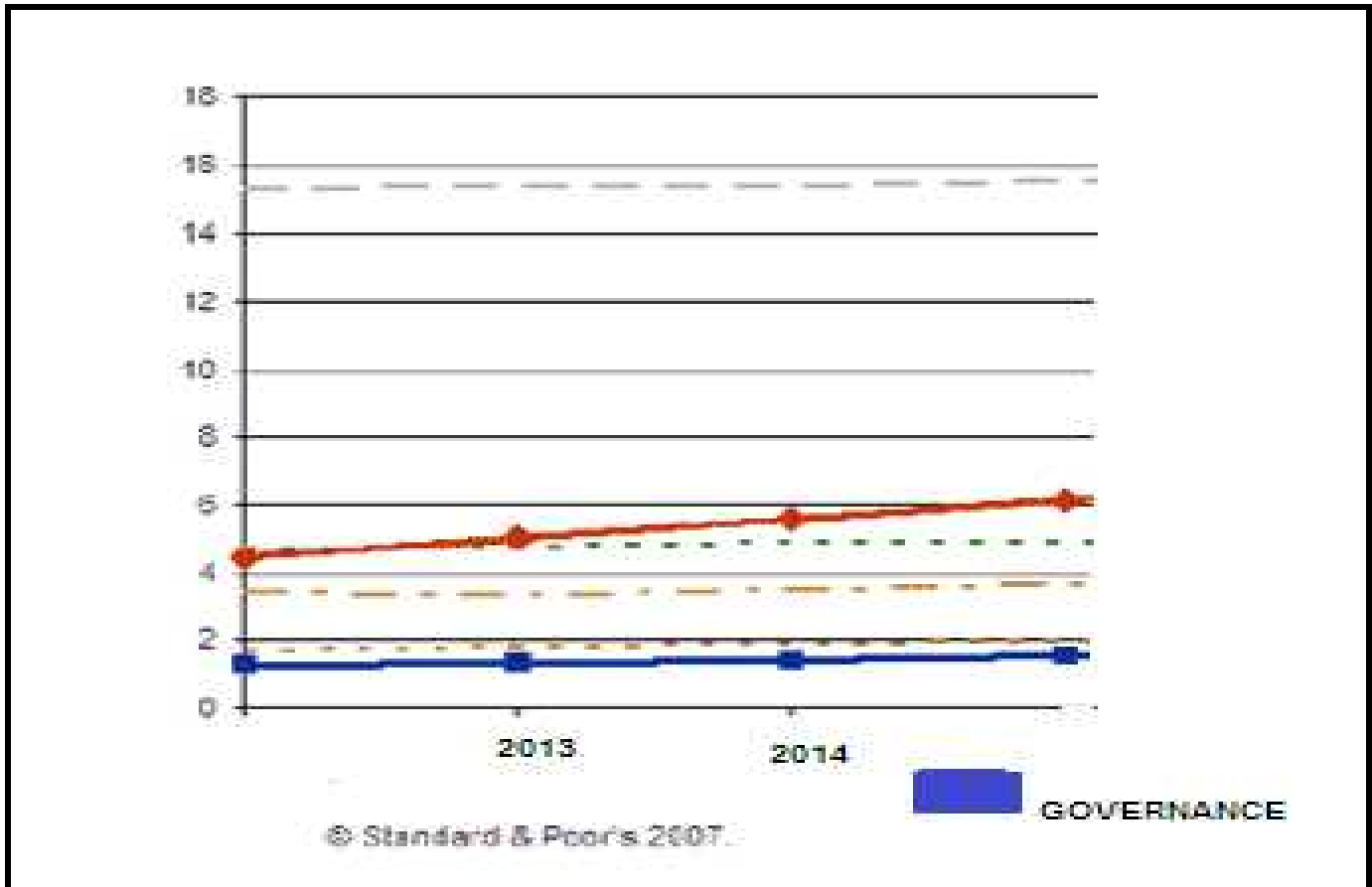
Figure II: Declining Trend in Governance Indicators of India in Pre-2013 Scenario



Source: Standard & Poor's Report (2014)

After the implementation of this new act in 2013, the credit ratings of India have gradually begun to improve as shown in Figure III. Still, it may be pointed out that just about half of the CPSEs in India could meticulously adopt the various guidelines on CG issued by the DPE under the Government of India, i.e. the 'Excellent' category cases of CPSEs. Moreover, there are yet many more CPSEs who are yet to reach the required benchmark set by DPE and about one-fourth of them are still in the 'Poor' grades as of now (2014) (Table I). In short, there is enough scope for improvement for India in the CG front even after the introduction of mandatory CG provisions since 2013. The post-2013 governance scenario (Figure III) should continue at still faster pace.

Figure III: Improving Trend in Governance Indicators of India in Post-2013 Scenario



Source: Standard & Poor's Report (2014)

7. MORE EFFECTIVE ADOPTION OF CG IN INDIA: SOME BROAD SUGGESTIONS

- The Vision, Mission and Values of each corporate entity should be given due respect on an ongoing basis. The management as well as employees at all levels should live up to these broad objectives on an ongoing and day-by-day basis, without fail.
- Going by the latest priorities of the Government regarding 'Inclusive growth' devoid of all kinds of divides, different stakeholders especially marginalized and excluded categories (e.g. women), workers etc. be given due representation in various bodies and committees.
- All CG initiatives should ideally seek to address the long-term and broader societal benefits as well as balanced and equitable development of the nation as a whole. The PSEs in particular have a special responsibility in this regard vis-à-vis other corporates, as PSEs are set up utilizing enormous funds of Governments at the Central and/or State levels.
- As a basic tenet, it shall be pointed out that every corporate entity, especially the PSEs, should look at CG not from the compliance perspective, rather the same needs to be done in its true letter and spirit for the long-term benefit of the society at large.
- Corporates, particularly the PSEs should good clarity as to the role of the Board regarding the strategy towards effective implementation of sound corporate governance practices.
- Side by side with the implementation of sound corporate practices corporate should ensure close monitoring of their organizational performance on an ongoing basis. Initiatives of every corporate should

strive to institutionalize such good practices that are broadly in conformity with the SEBI guidelines regarding corporate governance.

- It shall be ensured at all times that the Board of Directors (BOD) of all corporate have at their disposal the relevant information that they need for scientific and learned decisions. A skill-based BOD needs to be developed and maintained at all times by corporates.
- For efficient implementation of sound CG practices, corporate should ensure that an effective CG infrastructure is built up and maintained by them.
- Corporates should set up and maintain a permanent mechanism to evaluate the performance of the BOD and individual Directors on an ongoing basis, as well as to pursue opportunities for constant improvement thereof.

8. CONCLUDING REMARKS

In view of the foregoing, it may be noted that there has been commendable improvement in the setting up and maintenance of CG infrastructure in India, there are indications of a reversal of the declining trend in governance parameters since 2013. The efforts of the Government of India (GOI) to improve the CG performance of companies in general and CPSEs in particular, have been in the right direction. Indeed CG is the buzzword in all business circles today. Corporate governance is one of the pillars of focus on sustainability following environmental and social sustainability. Better corporate governance increases the likelihood that the enterprise will satisfy the legitimate claims of all stakeholders and fulfill its environmental and social responsibilities. Accordingly, it contributes to the long-term, sustainable growth of client companies. A company that is well-governed is one that is accountable and transparent to its shareholders and other stakeholders (such as employees, creditors, customers and the wider society).

In spite of such positive developments as above, it may be pointed out that even after the mandatory inclusion of the clauses of CG into the new Companies Act 2013, only about half of the CPSEs in India could attain the tag of 'Excellent' rating. This indicates that there is a need of more closer monitoring of the CG implementation process in India so as to ensure better CG practices in the country, particularly in respect of PSEs / CPSEs. There is indeed a long way for the DPE of the Government of India to traverse for the successful in implementation of CG in all PSEs in India. It has been a clear agenda for the Government that it would create more autonomy for PSEs and to try to make them at par with their private counterparts. This has made it much more necessary for the PSEs to adopt good CG practices so as to meet the challenges of the present market scenario. Let us hope that the GOI initiatives will continue in the future too and accordingly CG practices in Indian companies in general, particularly those in PSEs, will improve still further in the days to come.

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