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UNVEILING CORPORATE GOVERNANCE IN INDIA: NAVIGATING IMPACT AND EVOLUTION

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Abstract

This article gives an overview on corporate governance in India, focusing on key elements, challenges, and emerging trends. It explores the evolution of corporate governance practices in India, from traditional structures to contemporary frameworks, and assesses its impact on organizational performance, transparency, and stakeholder trust. Corporate governance is a system in which companies are controlled and directed. The study explores the rules that oversee how companies are managed in India. It focuses on organizations like the Securities and Exchange Board of India (SEBI) and the Ministry of Corporate Affairs. There are various social and cultural factors influencing the corporate governance in India. Indian companies often face challenges regarding establishing strong governance systems, composition of Board, conflict of interest and managing risks efficiently. The primary objective of this research paper is to discuss upcoming trends and possibilities for corporate governance in India, which includes sustainable governance, role of stakeholders in encouraging ethical business practices and using technology in governance methods.

Origin of Corporate Governance in India

Corporate Governance is a system of governance which guides the conduct of the people within an organisation and the direction of the organisation.[2] The scope of Corporate Governance in India is diverse and multifaceted.

In India, this concept can be traced long back to our ancient civilizations. Our ancient texts and scriptures like Vedas, Manu Smriti, Arthashastra, Neetistuti, etc. focuses on the ideas of good governance. The concept of good governance and stability are closely linked. This concept of good governance is not

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[2]Corporate governance in the United States (2019) ECGI. Available at: https://www.ecgi.global/content/corporate-governance-united-states (Accessed: 24 January 2024)

recently developed. It can be traced back to the Treta Yuga, during the time of Ramayana. The Ramayana is not just an epic which depicts the tale of love, it also demonstrates effective lessons on good governance.

When leaders listen to the people, take responsibility for their actions, can be replaced if needed, and can be recalled if they fail, it creates stability. Without these qualities, there is likely to be instability. These principles are still relevant today.

An individual needs to comply with the ethics being followed within the institution. Even Kautilya's Arthashastra clearly mentions the link between good governance and stability.[3]The concept of corporate governance is established on the grounds of certain principles. These principles are fairness, transparency, responsibility and accountability.

Although these principles can be found be in our texts, it was not in agenda of the Indian Companies until 1990s. In India, there were issues in the system, like unfair stock market practices, boards of directors not fulfilling their fiduciary duties, insufficient disclosure practices, lack of transparency, and ongoing issues with capitalism. These problems paved the way for several reforms as well as better governance practices in years to come.

Regulatory Authorities in India

The modern-day framework of corporate governance in India is fundamentally shaped by regulations and guidelines put forth by regulatory bodies, with an aim of enhancing accountability, transparency and ethical business conduct. The structure of corporategovernance in India has been crafted to align with international standards. Its emphasis revolves around the following aspects:[4]

● The basic framework for regulation of all companies in India is mentioned in the **Companies Act, 1956,** which provides for checks and balances over the powers of the Board of Directors.

● **The Companies Acts 2013** has provisions concerning Independent Directors, Board Constitution, General meetings, Board meetings, Board processes, Related Party Transactions, Audit Committees, etc.[5]

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[3]Corporate governance from ancient Indian scriptures: An overview - ICSI. Available at: https://www.icsi.edu/media/webmodules/CG_from_Ancient_Indian_Scriptures_AnOverview.pdf (Accessed: 24 January 2024)

[4]Corporate governance in India Legal Service India - Law, Lawyers and Legal Resources. Available at: https://www.legalserviceindia.com/legal/article-7435-corporate-governance-in-india.html (Accessed: 24 January 2024).

[5]Advocates, V.A. (2016) Corporate governance framework in India - shareholders - India, Corporate Governance Framework in India - Shareholders - India. Available at: https://www.mondaq.com/india/shareholders/456460/corporate-governance-framework-in-india (Accessed: 24 January 2024).

● **Securities and Exchange Board of India (SEBI)** plays a crucial role in regulating the securities market and ensuring the implementation of corporate governance practices. SEBI periodically issues guidelines and amendments to improve governance standards. SEBI provides protection to the investors and companies who follow the rules and regulations and work according to the guidelines.

● **Accounting Standards issued by the ICAI (Institute of Chartered Accountants of India)**:The ICAI is an autonomous body and issues accounting standards. The disclosure of financial statements is also made mandatory by the ICAI backed by the Companies Act 2013, Sec. 129.

● **Secretarial Standards Issued by the ICSI (Institute of Company Secretaries of India)** on 'Meetings of the Board of Directors','General Meetings', etc. The companies Act 2013 empowers this autonomous body to provide standards which each and every company is required to adhere to so that they are not punished under the Companies Act itself.

● **Standard Listing Agreement of Stock Exchanges** applies to the companies whose shares are listed on various stock exchanges.[6]

Challenges faced in Corporate Governance

Although the government, Securities and Exchange Board of India, and stock exchanges have made significant efforts to enhance corporate governance norms in India, particularly focusing on corporate boards. However, few critical issues persist:

● **Ownership Concentration:** A major concern is the concentrated ownership of corporations in India, often controlled by a single shareholder or a family, with promoter-run companies representing 45% of the market. This concentration poses governance challenges, allowing controlling shareholders to benefit at the expense of minority shareholders through practices like abusing related party transactions.[7]

● **Related Party Transactions (RPTs):** Related party transactions are deals between parties with preexisting relationships. In India, dominant shareholders may exploit RPTs to derive advantages, such as favourable pricing within their group of companies. This can lead to the improper extraction of corporate value.

● **Challenges with Independent Directors:** While Independent Directors were envisioned as a key governance reform, their impact has been limited. Promoters often remove them due to their passive role

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[6]ForumIAS (2018) Corporate governance framework in India: Analysis, Community. Available at: https://forumias.com/blog/corporate-governance-framework-in-india-analysis/#gsc.tab=0 (Accessed: 24 January 2024).

[7]Dr. Dr Jalwani, Pawan Kumar Bhura and Ashutosh Kumar Jha Available at: https://www.allcommercejournal.com/article/115/3-2-16-664.pdf(Accessed: 24 January 2024).

on boards. Despite regulatory strengthening, challenges persist in effectively addressing the role and removal of independent directors.

● **Ambiguous Corporate Governance Structure:** The concept of 'Corporate Governance' lacks a clear and universally accepted structure, resulting in ambiguity. Issues like financial disclosure quality, compliance with best practice codes, and the roles of Board of Directors remain areas of concern, with insufficient awareness.

●**Board Performance and Composition**: Requirements such as having at least onewoman director and maintaining a balance between executive and non-executive directors are not consistently met. Board performance evaluation is not conducted regularly, leading to a lack of transparency and result-oriented outcomes.

● **Accountability Beyond Shareholders**: Corporate accountability extends beyond shareholders to encompass society and the environment. Directors need to consider broader interests of all concerned stakeholders rather than solely focusing on their own personal motives. This aspect is crucial but not consistently prioritized.

● **Insider Trading Concerns:** Corporate insiders with access to confidential information may engage in insider trading. A lack of robust investigative mechanism and vigilant approach by SEBI allows wrongdoers to escape legal consequences.

● **Dominant Shareholder Conflicts:** Unlike in the US and the UK, the central problem in Indian corporate governance is conflicts between dominant and minority shareholders. Public sector units (PSUs) often witness governance abuses by the government, the majority shareholder, with nominal fines for non-compliance.

● **Misleading Financial Statements:** There are instances of presenting factually inaccurate information on financial statements in ways that mislead investors. Transactions like selling property from a parent company to a subsidiary may distort the actual financial picture.

● **CSR Implementation Challenges:** While CSR investment is mandatory, companies seem hesitant to allocate the required 2% of profits over the last three years. Encouraging CSR activities remains a challenge despite the regulatory mandate.

Way Forward

The four principles of corporate governance are fairness, transparency, responsibility and accountability.[8] Corporate governance is about being completely open, honest, and responsible. It involves the behaviour and actions of the management and executives. The rules introduced after the Companies Act 2013 have been fair and creative. Theyhave positively influenced the development of Indian companies in line with global standards. Shareholders play a significant role in company decisions, and protective measures are in place to ensure their interests and the well-being of society are not neglected.

While good corporate governance may not be the main factor driving economic growth, it does play a significant role in contributing to growth. If Indian companies adopt the best practices in corporate governance, it will attract the trust and investment of both local and international investors. It's important to note that regulations alone cannot ensure the success of a corporate governance system. There is a need to ensure that corporate governance structures are adaptable, flexible rather than fixed.[9] India does not need more regulation; it needs enforcement, which will lead to greater participation and transparency.

[8]Aeron, D. (2023) India's corporate governance – A brief, TaxGuru. Available at: https://taxguru.in/corporatelaw/indias-corporate-governance.html (Accessed: 24 January 2024).
[9]Supra Note 7