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Code And Laws For Corporate Governance

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Abstract:

The importance that has been laid in good corporate governance. Government, corporates and the civic societies have been doing their bit to improve upon the existing level of governance. Corporate governance goes beyond the realms of law. It comes from the culture, ethos and the mindset of management. However, due emphasis must be given to the role of legislation also. Need of the hour is to build an atmosphere of mutual trust, responsibility and accountability that makes the governing team enthusiastic and makes them aspire for excellence. Procedural refinements and innovation are no substitutes for 'good' men. while good men are never short of capacity to innovate. Thus, it is men more than measures that make good corporate governance for that matter 'the governance' give its true result.

Keywords: Reports of Committees on Corporate Governance, Government Initiatives, National Award Initiated by the Government of India, Recent Developments in Other Markets.

Introduction:

Any concept or idea to form a part of our existence or business needs to be put on paper in distinct terms, so that they are understood and followed by all in a similar fashion. These are called rules or codes of conduct. These are principles and standards that are intended to control, guide or manage behaviour or the conduct of individuals codes are self-imposed and regulations are imposed by the states.

There are many corporate governance codes developed by non-governmental organizations, stock exchanges, investor groups and professional associations. Government also issues rules concerning corporate governance through capital market regulatory body like SEBI and by enacting laws.

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Reports of Committees on Corporate Governance:

In the corporate world (throughout the world) raised concern about standards of financial reporting and accountability of management. Many believe that the failures could have been avoided had the companies followed good governance. In recent years, governments and corporates have made sincere efforts in designing and implementing codes for good corporate governance. Some of the reports on corporate governance published abroad and in India are:

- Cadbury Committee Report
- CII Committee Report
- Kumara Mangalam Birla Report
- Narayana Murthy Committee Report
- Cadbury Committee Report

The Cadbury Committee was set up in May. 1991 by the Financial Reporting Council the London Stock Exchange to address the financial aspects of corporate performance. The sponsors of the committee were concerned at the perceived low levels of confidence, both in the financial reporting and in the ability of auditors to provide safeguards which the users of the company reports sought and expected.

The Committee published its report and code of best practice in December 1992 From July 1993. all companies registered in the UK and listed on the London Stock Exchange have been obliged to state in their Annual Report.

The Code of Best Practice has been divided into four sections- the first concerning the role of the board of the directors and covering such matters as the duties of a board, its composition, the second dealing with the role of the outside non-executive directors, the third covering executive directors and their remunerations, and the final section addressing questions of financial reporting and financial controly. The major recommendations made by the committee are as follows.

- A single person should not be vested with the decision making power ie., the roles of chairman and chief executive should be separated clearly.
- The non-executive directors should act independently while giving their judgement on issues of strategy, performance, allocation of resources, and designing the code of conduct.
- A majority of directors should be independent non-executive directors, i.e., they should not have any financial interests in the company.
- The term of the director can be extended beyond three years only after the prior approval of the shareholders.
- A Remuneration Committee with majority of non-executive directors should decide on the pay of the executive directors.
- The Interim company report should give the balance sheet information and should be reviewed by the auditor.
- The information regarding the audit fee should be made public and there should be regular rotation of the auditors.
- An objective and professional relationship with the auditors must be ensured.

It must be reported that a business is a going concern.

CII Report:

The Confederation of Indian Industry (CII) took the initiative to draft some codes of corporate governance. A national task force on corporate governance was set up in mid 1996 under the leadership of Mr. Rahul Bajaj, ex. President, CII, and then CMD, Bajaj Auto Ltd. The committee issued desirable corporate governance. The major recommendations are as follows:

- At least 30% of the board (where the chairman of the company is non-executive) and 50% (where the position of the chairman and managing director is combined) of listed companies with a turnover of Rs.100 crores and more should comprise of professionally competent and independent non-executive directors.
- No person should hold directorships in more than 10 companies. In an earlier draft of the code this number was to exclude directorship on the company's subsidiaries (50% or more of equity holding) and affiliates (25% or more of equity holding).
- While re-appointing members of the board, companies should give the attendance record of the concerned directors. If a director has not been present (absent with or with out leave) for 50% or more meetings, then this should be explicitly stated in the resolution one should not re-appoint any director who has not had the time to attend even one half of the meetings.
- Non-executive directors should actively participate in board affairs and not be passive advisors, have clearly defined responsibilities within the board, and should be literate in understanding financials of the company.
- Non-executive directors should be adequately compensated through commissions and stock options.
- Board members should be provided timely and adequate information to enable them to discharge their duties.

Major Indian Stock Exchanges should gradually insist upon a compliance certificate, Signed by the CEO and CFO which clearly sates that the management is responsible for the preparation, integrity and fair presentation of the financial statements and other information in the annual reports.

Kumara Mangalam Birla Committee Report:

There is also an increasing concern about standards of financial reporting and accountability, especially after losses suffered by investors and lenders in the recent past, which could have been avoided, with better and more transparent reporting practices. Investors have suffered on account of unscrupulous management of the companies, which have raised capital from the market at high valuations and have performed much worse than the reported figures leave alone the financial projections at the time of raising money.

There are also many companies, which are not paying adequate attention to the basic procedures For shareholders service, for example, many of these companies do not pay adequate attention to redrest investors grievances such as delay in transfer of shares, delay in dispatch of share certificates and dividend warrants and nom-receipt of dividend warrants. SEBI has been daily receiving large number of investor complaints on these matters.

The Committee on Corporate Governance was set up on May 7,1999, by the Securities and Exchange Board of India (SEBI) under the Chairmanship of Shri Kumara Mangalam Birla, to promote and raise the standards of corporate governance. The purpose of the committee was,

1) To suggest suitable amendments to the listing agreement executed by the stock exchanges with the companies and any other measures to improve the standards of corporate governance in the listed companies, in areas such as continuous disclosure of material information, both financial and non-financial, manner and frequency of such disclosures, responsibilities of independent and outside directors,
2) To draft a code of corporate best practices, and
3) To suggest safeguards to be instituted within the companies to deal with insider information and insider trading.

Major recommendations of the committee are as follows.

- The board should have an optimum combination of executive and non-executive directors and at least 50% of the board should comprise of non-executive directors.
- No director should be a member in more than 10 committees or act as chairman of more than five committees in which he is a Director.
- The board of the company should set up a qualified and independent "Audit Committee".
- Board should set up a remuneration committee to determine the remuneration packages for the executives.
- The corporate governance section of the Annual Report should make disclosures on remuneration paid to directors in all forms including salary, benefits, bonuses, stock options, pensions and other fixed as well as performance linked incentives.
- Management should assist the board in its decision-making process in respect of company's strategy, policy, code of conduct and performance targets.
- The management should implement the policies and code of conduct of the board.
- It should provide timely, accurate, substantive and material information, including financial matters and exceptions to the board, board committees and the shareholders.

The committees also took note of various steps taken by SEBI for strengthening corporate governance, some of which are Stringent disclosure norms for Initial Public Offers.

- Stringent disclosure norms for Initial Public Offers.
- Providing information in director's reports for utilization of funds and variation between projected and actual use of funds as per the requirements of the Companies Act.

- Declaration of quarterly results.
- Mandatory appointment of compliance office for monitoring share transfer process.
- Timely disclosure of material and price sensitive information having a bearing on the performance of the company.
- Dispatching one copy of complete balance sheet to every household and abridged balance sheet to all shareholders.
- Issue of guidelines for preferential allotment at market related process.
- Issue of regulations providing for a fair and transparent framework for takeovers and substantial acquisitions.

The recommendations made by Shri Kumara Mangalam Birla Committee were accepted by SEBI in December 1999, and are now enshrined in Clause 49 of the Listing Agreement of every Indian stock exchange.

Narayana Murthy Committee:

The Narayana Murthy Committee has mentioned about correct approach for successful corporate governance. It has said:

"Corporate Governance is beyond the realm of law. It stems from culture and mindset of management, and cannot be regulated by legislation alone. Corporate govern deals with conducting the affairs of a company such that there is fairness to all stakeholders and that its actions benefit the greatest number of stakeholders. It about openness, integrity and accountability. What legislation can and should a to lay down a common framework the "form" to ensure standards. The 'substance will ultimately determine the credibility and integrity of the process. Substance inexorably linked to the mindset and ethical standards of management."

Some of t major recommendations made by the committee are as under:

- All audit committee members should be 'financially literate' and at least o member should have accounting or related financial management expertise.
- Mere explanation as to why a company has followed a different accounting standard from the prescribed standards will not be sufficient.
- Board members should be informed about risk assessment and minimization procedures.
- Board members should be trained in the business model of the company a as the risk profile of the business parameters, their responsibilities as dire and best ways to discharge them.
- Use of proceeds of IPO should be disclosed to the audit committee.
- There shall be no nominee directors when a director is to be appointed on the board and shareholders shall make such appointments.
- Board of Directors, limiting the maximum number of stock options that can be granted to non-executive directors in any financial year, may fix compensation paid to non-executive directors.

Naresh Chandra Committee:

On 21 August, 2002, the Department of Company Affairs (DCA) under the Ministry of Finance and Company Affairs appointed a committee under chairmanship of Shri Naresh Chandra to examine various corporate governance issues. The committee has been entrusted with analyzing and recommending changes if necessary, in various areas, like, statutory auditor-company relationship, independence of auditing functions, certification of accounts and financial statements by managers and directors, adequacy of regulation of chartered accountants, company secretaries, cost accountants, and other similar statutory oversight functionaries, the role of independent directors, etc. The committee recommended detailed regulations on auditor's independence, working of audit committees, board composition and governance.

Government Initiatives:

There have been swift moves through law and regulations made by the Department of Company Affairs (DCA) and Securities and Exchange Board of India (SEBI) to hasten the process of bringing improvements in the Corporation's functioning. The DCA has amended Companies Act at short intervals for this purpose. Number of provisions in the Companies Act, 1956 concerning corporate governance have been inserted in the Act through Companies (Amendment) Act 2000. Important changes to improve corporate governance in this act are:

- Providing for Director's Responsibility Statement (Section 217(2A)).
- Board to report in cases where buyback was not completed within the time specified in sub-section (4) of Section 77.
- Small shareholders to get representation through Director (Section 252).
- Limitations in Directorship in companies (Sections 274 & 275).
- Constitution of Audit Committees (Section 292A).
- Providing for higher penalties (tenfold increase) for offences provided in various sections of the Companies Act etc.

The Amending Act of 2000 thus increased manifold, the duties and responsibilities of the Directors in the companies as a step to improve the corporate governance.

National Award Initiated By the Government of India:

There has been considerable debate on the importance of good governance of Indian corporates. It is increasingly being realized that if investors have to be driven back to the capitol market, companies have to put their houses in order by following internationally accepted practices of corporate governance. This is necessary to enhance investor confidence.

In order to promote good governance practices in Indian companies and enhance investors confidence in the market, the Government of India awards the National Award for Excellence in Corporate Governance every year. The Award is recommended by a Panel consisting of eminent persons from financial market and corporate world.

In the year 1999 the panel constituted for the purpose initially short-listed the following nine criteria for evaluation.

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1. Adequate representation of independent directors on the Board.
2. Existence of institutions, like audit committee, which enable the Board to adequately guide the management.
3. Adherence to prescribed accounting standards and quality of disclosures relating to financial and other information provided to shareholders in the Annual Reports.
4. Frequency and content of communication of financial and operating data to the shareholders and to the public.
5. Investor-friendly procedures and practices.
6. Enhancement of shareholder value vis-à-vis the industry performance.
7. Discharge of social obligations and obligations related to employee welfare.
8. General concern for the environment.
9. Ethical code of conduct.

The following two criteria were added to the list.

1. HRD policies for succession, delegation, and empowerment of employees.
2. Innovative practices to improve quality of life for other stakeholders of the company.

Based on these criteria the following Companies were nominated for the consideration for the Award;

1. Agrevo (India) Ltd.	2. Archies Greetings and Gifts Ltd.
3. Asea Brown Boveri Ltd.	4. Asian Paints Ltd.
5. Bajaj Auto Ltd.	6. BFL Software Ltd.
7. Bharat Forge Ltd.	8. BPCL
9. Britannia Industries Ltd.	10. BSES Ltd.
11. Cadbury India Ltd.	12. Castrol India Ltd.
13. Cipla Pharma Ltd.	14. Colgate India Ltd.
15. Container Corporation of India L.	16. Corporation Bank
17. CRISIL	18. Dabur India Ltd.
19. Pigital Equipment India Ltd.	20. Dr. Reddy's Laboratories Ltd.
21. EIH Ltd.	22. Finolex Cables Ltd.
23. Finolex Industries Ltd.	24. GACL
25. Glaxo India Ltd.	26. Global Telesystem Ltd.
27. HCL Infosystems Ltd.	28. HCL Technologies Ltd.
29. HDFC Bank Ltd.	30. HDFC Ltd.
31. Hero Honda Motors Ltd.	32. Hindalco
33. Hindustan Lever Ltd.	34. HPCL
35. ICICI Lad.	36. Indian Hotels Company Ltd
37. Indian Oil Corporation	38. ITC Ltd.
39. Larsen & Toubro Ltd.	40. Lupin Laboratories Ltd.
41. Mahindra & Mahindra	42. Mphasis BFL. Ltd.
43. Motor Industries Company Ltd.	44. MRF Ltd.
45. Nicholas Piramal India	46. NIIT Ltd.
47. Novartis India Ltd.	48. ONGC
49. Pidilite Industries Ltd.	50. Procter & Gamble India Ltd.
51. Punjab Tractors Ltd.	52. Ranbaxy Laboratories Ltd.
53. Reckitt & Coleman India Ltd.	54. Reliance Industries Ltd.

55. Satyam Computers Ltd.
56. SmithKline Beecham India Ltd.
57. State Bank of India
58. Sun Pharmaceuticals Ltd.
59. Sundaram Fastners Ltd.
60. TVS Suzuki Ltd.
61. VSNL
62. Wipro Ltd.
63. Wockhardt Ltd.

Recent Developments in Other Markets:

Implementation of Sarbanes-Oxley Act, 2002 in the U.S.A.

The public outcry against the recent corporate scandals like, Enron. World Com, etc, a new legislation viz, the Sarbanes-Oxley Act has been enacted on July 30, 2003 in the US.A. in order to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws. The legislation initiated major reforms in the following areas

1. Public Company Accounting Oversight Board
2. Auditor's independence
3. Conflict of interest
4. Corporate responsibility
5. Enhanced financial disclosures
6. Analyst conflict of interest
7. Corporate and criminal fraud accountability
8. White-collar crime penalty enhancements
9. Corporate fraud and accountability
10. Studies and reports

European Union:

The European Commission recently completed a study of 43 different corporate governance codes and proposed to merge all of them to create a single, consistent code

Germany:

The German government had announced details of comprehensive new voluntary guidelines to improve their corporate governance practices. The code aims at strengthening the rules concerning auditor and supervisory board independence, gives shareholders a limited role in takeovers, recommends that companies disclose board remuneration individually, and requires a company to disclose whether or not they comply with the code.

Ireland:

Irish Association of Investment managers revealed a high level of compliance amongst Irish corporates with the Combined Code on governance implemented by LSE. 97% of firms allow shareholders to vote on re-election of directors every three years. 85% and 79% of them have remuneration and audit committees respectively comprised fully of non-executive directors. 79% of them have separate role for the chairman and the chief executive officer

Asian and Latin American Markets:

S&P carried out a survey of 350 Asian and Latin American companies on 10 points based on 98 information attributes grouped into 3 categories: financial transparency and information disclosures; ownership structure; and board and management structure and practices. 19 out of 43 Indian companies managed to get score of 4; Infosys scores 7.

Kenya:

Kenya's Capital Market Authority has introduced new guidelines to improve corporate governance practices. The

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guidelines include: appointment of independent directors, constitution of nomination committee, the role of CEO and Chairman to be separated; limiting the term of director on the board subject to shareholders' approve and frequent appraisal of the board.

Thailand:

Stock Exchange of Thailand is set to introduce a new committee to strengthen corporate governance and make best corporate practice a national priority. Thailand's SEC has drafted a framework for corporate governance ratings aimed at protecting shareholders' rights, the quality of directors and the efficiency of internal controls. The Thai SEC will offer highly rated firms bunch of incentives, including a fast-track review of their corporate filings to issue new shares.

Russia:

Russia's Federal Commission for Securities Markets introduced new code of corporate governance which includes a number of tax incentives and investor friendly regulations.

Hong Kong:

Hong Kong's SEC proposed a rule that executives who intentionally or recklessly, provide false or misleading information in public disclosures, shall face up to two years in prison and a HKD 1 million fine.

Philippines:

Philippines SEC has requested that all listed firms establish an evaluation system to track performance of their boards and executive management. The recently approved code of corporate governance recommends that all public entities and fund raising entities shall adopt the same. Philippines' SEC is likely to extend new corporate governance code to require even non-listed firms to place at least one independent director on the board.

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