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An Analysis of Corporate Governance Regime in India: A Success or Failure

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ABSTRACT

Corporate governance refers to the set of laws, regulations, and procedures that govern organizations. It comprises carrying out the firm's business activities in line with the desires of its stakeholders or in the company's and its stakeholders' best interests. As the size of the finances and the opulence of corporate entities increased over time, the highly desired qualities began to be neglected, and those occupying high positions in these corporate entities began to take extreme measures to maximize the company or individual profits by engaging in extra-legal, unethical, and corrupt practices. Along with the other countries India has also seen financial scandals of higher degree throughout the recent past like the frauds involving Harshad Mehta and Khetan Parekh, Neerav Modi, and many more. These frauds have proven that corporate governance has failed despite several checks by regulating authorities like SEBI etc. Several efforts and new provisions are added by the Companies Act ,2013 but it is more important that the implementation of these rules is also done diligently.

***Keywords**: Corporate Governance, Company Law, Independent Directors, Corporate Social Responsibility, Corporate Frauds.*

I. INTRODUCTION

The system of rules, policies and processes that regulate organizations is referred to as corporate governance. It entails conducting the firm's business operations in accordance with the wishes of its stakeholders or the best interests of the company and its stakeholders.

Corporate governance can range from a small collection of rules and procedures followed by a few individuals to a large institution with numerous strategic wings and governing divisions with a network of functionaries, depending on the size and scale of operations of the organization. The best interests of all stakeholders are what corporate governance seeks to achieve. Initially, everything was seen from the purview of shareholders but the development

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of corporate governance emanated from the term stakeholders.

Stakeholders are the persons who are connected with the company either directly or indirectly or who have interests be it personal, professional, or financial in the company. They could be either internal or external stakeholders. Where we can say that promoters, shareholders, employees, executives, and others are included in internal stakeholders, Customers, Creditors, dealers, vendors, regulatory bodies, and governing authorities can be taken as a few examples of external stakeholders.

Even though a company is said to be a separate legal identity, its personality has certain limitations when it comes to performing particular duties. It is only a legal creature that only exists in the legal sense and is unable to make certain choices that set natural beings apart. Making decisions and managing the company's affairs are two things that a corporation cannot do on its own. Hence to comply with these functions a company needs a body of natural beings. This group of people is known as the board of directors.

Directors even though are one of the most imperative members of a company but they are not the only ones. There are several other people associated with the company, tagged as key managerial personnel (KMPs) like high managerial offices of a company such as the Chief Executive Officer (CEO), Managing Director (MD), Manager, Company Secretary (CS), whole-time director, Chief Financial Officer (CFO) as mentioned under the companies Act,2013[4]and other stakeholders. Some of the famous definitions of corporate governance are:

According to the UK's Cadbury Committee, corporate governance is as follows:

> *"(It is) the system by which companies are directed and controlled."*[5]

The Kumar Mangalam Birla Committee, which was established by SEBI, noted [6]

> *"Strong corporate governance is indispensable to resilient and vibrant capital market and is an important instrument of investor protection. It is the blood that bills the views of transparent corporate disclosure and high quality accounting practices. It is the muscle that moves a viable and accessible financial reporting structure."*

The SEBI-appointed N.R. Narayana Murthy Corporate Governance Committee has noted that [7]

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[4] Section 203, The Companies Act 2013, Acts of Parliament, 2013 (India).

[5]*Definition of Corporate Governance*, (June 15, 2023) https://www.applied-corporate-governance.com/definition-of-corporate-governance/.

[6]*Report of the Committee Appointed by the SEBI on Corporate Governance under the Chairmanship of Shri Kumar Mangalam Birla*, (June 15, 2023) https://www.sebi.gov.in/sebi_data/commondocs/corpgov1_p.pdf.

[7] *The Report of Shri N R Narayana Murthy Committee on Corporate Governance*, (July 15,2023) https://www.sebi.gov.in/reports/reports/mar-2003/the-report-of-shri-n-r-narayana-murthy-committee-on-corporate-governance-for-public-comments-_12986.html.

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

The word "corporate governance" is also defined by the Institute of Company Secretaries of India as follows:: [8]

"Corporate Governance is the application of best management practices, compliance of law in true letter and spirit and adherence to ethical standards for effective management and distribution of wealth and discharge of social responsibility for sustains development of all stakeholders."

Analyzing the above definitions given by different committees and organizations we can say that corporate governance is much broader as a concept and goes beyond the scope of corporate law. Corporate governance is a complex topic. An imperative motif of corporate governance deals with matters of amenability and a fiduciary duty primarily bolstering the application of rules and mechanisms to endorse reverence and safeguard shareholders. The efficiency perspective, the means by which corporate governance structure should attempt to optimize fiscal outcomes, is another significant focus.

As the size of the finances and the opulence of corporate entities increased over time, the highly desired qualities began to be neglected, and those occupying high positions in these corporate entities began to take extreme measures to maximize the company or individual profits by engaging in extra-legal, unethical, and corrupt practices.[9]

If corporate governance is taken into account in this situation, thoughts will undoubtedly turn to the implosion of enterprises owing to a dearth of virtuous management in some situations, a paucity of personnel with sufficient expertise to advise in some circumstances, and, most importantly, persons who engaged in illegal activities to deceive the company, the public, corporate affairs, and enforcement authorities.

II. NEED FOR CORPORATE GOVERNANCE IN INDIA

Along with the other countries India has also seen financial scandals of higher degree

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[8] *ICSI recommendations to strengthen corporate governance framework*, (August 05,2023) https://www.mca.gov.in/Ministry/latestnews/ICSI_Recommendations_Book_8dec2009.pdf.
[9] S.K. VERMA, & SUMAN GUPTA, CORPORATE GOVERNANCE AND CORPORATE REFORMS IN INDIA, 1st ed. 2004)

throughout the recent past like the frauds involving Harshad Mehta and Khetan Parekh, Neerav Modi, and many more. Prior to 1991, only a small number of Indian businesses were professionally run; the majority were run by family groupings. The liberalization movement that began in 1991 has necessitated a lot of attention to excellent corporate governance principles in order to compete with global market standards.

India is rapidly becoming one of the world's fastest-growing economies. Today, Indian businesses are among the best in the developing world. Many Indian businesses are reorganizing to become international corporations by making investments abroad and setting up their offices or subsidiaries. Customers, employees, investors, the government, and society are just a few of the many stakeholders that make up a firm. An Indian corporation must treat its stakeholders fairly and transparently in all of its transactions under the new circumstances. The necessity for firms to access global financial resources, recruit and retain the greatest human capital from across the globe, work with retailers on large associations, and live in peace with the community has made this an essential issue in today's business environment.

Corporations must understand that all stakeholders must participate in their success, and that adherence to the highest standards of corporate governance fosters this cooperation. Additionally, the management must serve as the shareholders' trustee and watch out for the distribution of disproportionate benefits to various owner groups, particularly between owner-managers and the other shareholders.

Due to recent corporate scams that occurred despite a number of preventative measures, such as laws, rules, and regulations, the notion of "Corporate Governance" has become more important. Because of the rising level of failure that is seriously harming not only the interests of ordinary investor shareholders but also the entire economy, there is growing worry about the necessity of employing this notion in business domains. [10]

The notion of corporate governance grew in prominence as corporations were forced to improve their performance and financial markets began to integrate. To compete with the best in the world, intermediaries, and other fund managers, fund managers were bench-marked against each other. Investors who were previously somewhat passive had to become 'activists' in order to maintain their market share. The ability of the investor to make their own decisions has been crucial in the development of corporate governance.

The Companies Act of 2013, the Monopolies and Restrictive Trade Practices Act of 1969, the

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[10] Dilip Makwana, *Globalization and Changing Trends of Corporate Governance in India, R.N. Sharma (ed.),* 27 IJLS 90, (2009).

Competition Act of 2002, the Foreign Trade (Development & Regulation) Act of 1992, and the Foreign Exchange Management Act of 1999 primarily regulate India's corporate sector. The Securities and Exchange Board of India Act, 1992, together with any ensuing rules, regulations, and guidelines, also apply to listed firms. Even then, corporate offences are not entirely prohibited due to the lack of implementation of these acts.

That’s the reason good governance has become more important. Corporate governance is a notion that translates into administering a company's affairs in a way that provides fairness to the consumer, investor, vendor, government, and society as a whole. The topic of corporate governance has several facets. The commencement of corporate developments in India was distinguished by the managing agency structure, which fostered widespread equity ownership but also the practice of giving managers control rights that were disproportionately greater than their stock ownership. A system and culture of licencing, protection, and extensive red tape were established by the 1951 Industries (Developments and Regulation) Act and the 1956 Industrial Policy Resolution, which were indicators of the shift towards socialism in the decades after independence. These laws and regulations encouraged corruption and restrained the growth of the corporate sector.

Over the ensuing decades, the situation deteriorated rapidly, and the Indian corporate sector came to be known for its corruption, nepotism, and incompetence. Exorbitant tax rates prompted innovative accounting techniques and complex remuneration arrangements as a means of evading the law.

In India, boards of directors have been largely ineffectual at supervising management's conduct. They are routinely crammed with acquaintances and supporters of the promoters and managers, in egregious infraction of the purport of company law. The Indian equity markets were neither liquid nor developed enough to exert meaningful oversight over the corporations during the majority of the post-Independence era. Stock Exchange listing rules imposed some transparency, however, non-compliance was neither uncommon nor dealt with.

Overall, despite the existence of numerous rules, minority shareholders and creditors in India continued to be essentially unprotected.

The Companies Act 2013 is supportive of corporate governance and has a number of provisions that will aid in fostering stronger corporate governance in the coming years. The Act, among other things, places a priority on sound corporate governance practices by expanding the Board's functions and responsibilities, safeguarding shareholders' interests, implementing a disclosure-based regime, and introducing self-regulatory mechanisms with built-in deterrence.

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The 2013 Act fundamentally alters how businesses are governed. The improvements to corporate governance brought about by the current act can be discussed in the following heads:

(A) Independent Directors

The phrase "independence" was given a relatively restrictive interpretation in the Indian corporate regime from its beginning. The term "independent directors" was first defined by the Kumar Mangalam Birla Committee as follows:[11]

> *"Independent directors are directors who apart from receiving director's remuneration do not have any other material pecuniary relationship or transactions with the company, its promoters, its management or its subsidiaries, which in the judgement of the board may affect their independence of judgement."*

According to the definition, it considers solely monetary interests, which is an exceedingly narrow approach. This is especially constraining in the Indian setting given the importance of familial and social relationships in the corporate environment.

Section 149(4)[12], Companies act 2013 read along with rule 4 of the Companies (Appointment and Qualification of Directors) Rules,2014 prescribes the minimum number of independent directors. Several provisions of the Act contradict Clause 49 of the Listing Agreement, which all listed firms are expected to follow. The potential Independent Director's relationship with the company's Promoters or Directors is one of the requirements listed in the Act that must be met before a person may be appointed as an Independent Director. The Act does not contain the clause in the Listing Agreement that requires Independent Directors to make up at least one-third of the Board in circumstances where the non-executive chairman is a promoter or anyone holding management responsibilities at the Board level or one below the Board. In circumstances when a non-executive chairman is a person holding managerial roles at the Board level or one below the Board, it also stipulates that at least one-half of the Board must be independent.[13]

The Act has set apart Independent and Non-Executive Directors' liability from that of the rest of the Board. The Act limits an Independent Director's culpability to all such omissions or commissions by a firm that occurred with his knowledge, are attributable to him through board

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[11] *Supra* note 6.

[12] Sec. 149(4), The Companies Act 2013, Acts of Parliament, 2013 (India) "*Every listed public company shall have at least one-third of the total number of directors as independent directors and the Central Government may prescribe, the minimum number of independent directors in case of any class or classes of public companies.*"

[13] *Corporate Governance in listed Companies - Clause 49 of the Listing Agreement*, (29th August,2023), https://www.sebi.gov.in/legal/circulars/oct-2004/corporate-governance-in-listed-companies-clause-49-of-the-listing-agreement_13153.html.

processes, with his approval or connivance, or where due diligence was lacking. The director is required to provide evidence.[14]

The majority of independent directors are unable to effectively carry out their jobs and responsibilities because they are reluctant to compromise the collegiality of group decision-making. It was widely believed that Independent Directors were not involved in the operations and management of a company and were hired to protect proper corporate governance. Two significant Supreme Court rulings essentially addressed this controversy. According to the Supreme Court's ruling[15], a person must meet both the legal and factual requirements of being a person in law responsible for the conduct of the company's business in order to be found legally responsible for an offence.

> *"to be vicariously liable under sub- section (1) of Section 141, a person should fulfill the 'legal requirement' of being a person in law (under the statute governing companies) responsible to the company for the conduct of the business of the company and also fulfill the 'factual requirement' of being a person in charge of the business of the company."*

So we can say that the Court offered two tests: the fact-based test and the test based on the statute. It is necessary to prove that a person is in charge of how the corporation conducts its business under the statute-based test. The appellant must prove that the individual person had total control over the day-to-day operations of the business in order to pass the second fact-based test. Therefore, a person is not obliged to pass the second test if they fail the first one.

In the case of S.M.S. Pharmaceuticals[16], the Supreme Court made the same declaration, stating that responsibility for the company's operations at the time the offence was committed puts one at risk for liability rather than merely holding a position of authority within the organisation:

> *"Merely being a director of a company is not sufficient to make the person liable under Section 141 of the Act. A director in a company cannot be deemed to be in charge of and responsible to the company for the conduct of its business. The requirement of Section 141 is that the person sought to be made liable should be in charge of and responsible for the conduct of the business of the company at the relevant time. This has to be averred as a fact as there is no deemed liability of a director in such cases."*

[14] Section 149(12), The Companies Act 2013, Acts of Parliament, 2013 (India)
[15] K.K. Ahuja v. v. K. Vora , 2009 (3) CC (NI) 194(India).
[16] S.M.S. Pharmaceuticals Ltd. v. Neeta Bhalla and Others, (2005) 8 SCC 89(India).

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III. Corporate Social Responsibility (CSR)

Another important initiative of the 2013 Act is the introduction of CSR[17]. The 2013 Act attempts to instil a culture of corporate social responsibility (CSR) in Indian businesses by mandating them to create a CSR policy and spend at least a predetermined amount on charitable endeavours. The term "CSR," also referred to as "corporate responsibility," "corporate citizenship," "responsible business," "sustainable responsible business," or "corporate social performance," refers to what some see as a company's obligation to consider the needs of all of its stakeholders in its business operations.[18] The social responsibility of corporates comprises the economic, legal, ethical, and discretionary expectations that society has of organizations at any particular time.[19] The term "social responsibility of business" has now taken over business jargon and is frequently used in conversations and disputes. The strongest guarantee for long-term peace, stability, and social cohesion is profit with a purpose greater than one's self-interest, which is absolutely important for firms to operate without restraint. Businesses can act responsibly toward society if they perform two things, as has been highlighted with justification. First and foremost, they must refrain from taking any action that could intentionally harm their stakeholders, including their customers, suppliers, employees, investors, and the local community in which they operate. Second, businesses must make amends if the wrongdoing is uncovered and brought to their knowledge if they inflict harm to their stakeholders.

Due to numerous significant oversight mistakes and frauds, good governance has become more broadly defined to include ethical aspects. Successful values are at the heart of good administration, and it is crucial to both declare and uphold these principles. One could say that corporate social responsibility is an outward manifestation of these ideals. In order to integrate the value dimension, corporate governance typically departs from the traditional primary governance function. It goes without saying that the most crucial aspect of the governance process is deciding what sort of corporate citizen the firm aspires to be. Corporate Social Responsibility is intimately related to this effort. Corporate social responsibility is a growing trend today. It is reasonable to presume that this is the area for talking about corporate responsibility.

IV. Failure of corporate governance: few cases

There are many cases in India that show how corporate governance has failed from time to time.

[17] Section 135, The Companies Act 2013, Acts of Parliament, 2013 (India).
[18] , Anas Mohammed Riyaz & Suvir Sharma, *Corporate Social Responsibility: Perspective Difference among Developed and developing Nations*, 3 Comp LJ 49,(2010).
[19] Archie B Carroll, *A Three-Dimensional Conceptual Model of Corporate Performance*, 4 AMR, 500 (1979).

Harshad Mehta stock market crash or kingfisher airlines scam or Nirav Modi -PNB scam, the list of such failure of governance cases is very big. Satyam Scam is one of the biggest corporate governance failure case and Tata and sons and Cyrus Mistry the recent most talked about corporate governance case.

- Satyam Scandal[20]

The scandals in any domain are often wraped. They betoken in for the catastrophic failures that are "visible." A thorough examination and analysis of India's Enron, Satyam Computer's "creative- accounting" scandal shows that their affair has raised serious concerns about India's whole corporate governance framework. The various governmental oversight organisations are consequently launching investigations into this form of "creative" accounting that results in fraud in publicly traded corporations.

It has never been simple to examine the Satyam Scam. It has its own complexity because the subject includes a 14000 crore swindle. Even today, the Satyam Scam is used as an illustration of poor corporate governance practises. Any business's core relationship—that between stockholders and employees—has never been fulfilling.

So, reading this case study is really necessary if one want to shed light on the subpar governance practises of one of the big IT firms. The Satyam Scandal essentially emphasises the significance of Corporate Governance and Securities Law in emerging nations. Due to Satyam's failure to uphold its duties to its numerous stakeholders, a problem with corporate governance developed. This case raised concerns and questions about major governance issues like: separation of the CEO and chairman's responsibilities; appointment to the board; director and executive compensation; diffident role of auditors and protection of shareholders' and their executives' rights.

Satyam scam had a humongous impact. The stock market collapsed, shareholders suffered huge losses, around 50,000 people were on the verge of losing their jobs and this also had an impact on India's GDP. This scam proved that even though laws and acts are there but the implementation needs to be more stringent. Corporate frauds like this, as well as the public need for pellucidity and candor in reporting, have resulted in two results. In order to unravel the intricate accounting techniques that have obscured financial statements, forensic accounting expertise has become very essential. Second, public pressure for change, followed by regulatory action, has revolutionised the global Corporate Governance picture.

[20] Satyam Computer Services ltd v. Central Board of Direct Taxes and others, SLP (C) No. 9590 of 2011.

- Tata Consultancy Services Ltd. Case[21]

Another important case study highlighting the failure of corporate governance in the most recent era is the high-profile legal battle between Cyrus Mistry and Ratan Tata. The present dispute highlighted the trust issues, and raised concerns of minority shareholders highlighting corporate governance failure when the Cyrus Mistry was removed from his position without following proper rules as alleged by Mistry. But the supreme court in its judgment gave clean chit to Tata and sons after analysing in depth the definition of oppression and mismanagement along with the right of the tribunal in the company's internal matters.

Cyrus Mistry and Ratan Tata's five-year-long and high-profile corporate legal dispute interpreted section 241 of the Companies Act, 2013 and its applicability. In addition, the judgment provided a succinct overview of the authority of the Company Law Tribunal and held that, with the exception of situations in which the expulsion of an individual as Chairman of a company is "oppressive or detrimental in nature," the Company Law Tribunal cannot impede with such expulsion. The only issue that arose—there was never even a case—was Cyrus Mistry's dismissal as chairman of Tata Sons Limited. On October 24, 2016, Cyrus Mistry was fired from his position as executive chairman of Tata Sons Limited. Rather than out of concern for Ratan Tata's comfort, this was done because Cyrus Mistry's abilities to manage the company was no longer regarded as a strong asset by the majority of the company's shareholders and board of directors.

V. Conclusion

Corporate governance is a requirement for the development of capital markets in developing countries. Investor participation in corporate securities may only be promoted when reliable corporate governance is in place and working well. Without it, investors will not seem to invest in businesses and private limited firms will not seem to issue their shares on stock exchanges. As a result of increased competition and globalisation, Corporate Governance necessitates limitations on the Board of Directors' responsibility, controllership, and reporting functions, as well as embracing the interaction amongst multiple participants in defining the company's direction and performance. The establishment of a proper and workable relationship between a company's various contributors, the Board of Directors, and other stakeholders is also required.

India is not an exception to the profound shifts in core assumptions occurring in other economies. We need some consistency in light of the widespread fundamental changes and the

[21] Tata Consultancy Services Ltd. Case v. Cyrus Investment Pvt. Ltd, (2021) SCC Online SC 272(India).

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governmental protections being loosened in sectors like insurance, banking, and power, among others. In these turbulent times, it is crucial to concentrate on corporate governance. Corporate governance standards that are broadly adopted will make businesses stronger in the long run. Corporate governance best practises are now a must in India; the question is more a matter of "how" and "how soon."

The moment is perfect for Indian companies to adhere to the rules of corporate governance. There are many Indian organisations that are adhering to the current corporate governance compliance, including Reliance, ICICI, Infosys, HDFC, etc. However, the bulk of Indian corporations have more work to do in this area. The study makes it abundantly evident that all efforts toward globalisation can only be realised through corporate governance, making corporate governance a necessary condition for both globalisation and the development of any country. Modern businesses' contributions to society support their claims to be social institutions. They help the unemployed in society find work, ensuring one's own and their families' financial security. Corporations provide goods and services in order to meet the demands of their customers. They give investors the chance to profit from their investments. By maintaining the business's vital systems, they make sure that their suppliers do not go out of business. They essentially meet the majority of socioeconomic needs.

Transparency and a positive working relationship between stakeholders and firm managers are crucial for corporate governance success. There have historically always been justifications for "beating the system" and dishonest corporate governance methods. As a result, corporate executives who are unwilling to change their roles typically oppose transparency and accountability. Market forces cannot be relied on to ensure change in corporate practises in India, or in any secure environment. Any changes to corporate governance would be made with very little formality. Now that good corporate governance is understood, there is a need for a supervisory instrument that will ensure active monitoring.

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