International Journal for Multidisciplinary Research (IJFMR)
E-ISSN: 2582-2160 • Website: www.ijfmr.com • Email: editor@ijfmr.com

Beyond Regulation: A Jurisprudential Inquiry into the Normative Foundations of Corporate Governance in India

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ABSTRACT

The concept of corporate governance has evolved significantly, especially in response to corporate scandals, financial crises, and the growing complexity of business operations. To understand why corporate governance requires regulation, the article delves into past instances of corporate fraud and mismanagement in India and abroad. Regulatory mechanisms provide the necessary oversight, enforce compliance, and build public trust. This justifies the proactive role of statutory bodies and governments in shaping corporate behavior. The article further elaborates on corporate governance reforms in India, with a focus on legal and regulatory frameworks. It discusses key legislation, including the Companies Act, 2013, which introduced several governance-related provisions such as the role of independent directors, board committees, disclosure requirements, and enhanced accountability. A detailed analysis of the Securities and Exchange Board of India (SEBI) regulations is also included, particularly the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, which apply to listed entities and enforce stringent standards of disclosure, board composition, and shareholder rights protection. Through a comprehensive examination of conceptual foundations, legal frameworks, and regulatory developments, this article aims to contribute to the ongoing discourse on enhancing corporate governance in India. It underscores that good governance is not just about compliance, but about fostering a corporate culture of integrity, transparency, and accountability.

Keywords: Corporate Governance, SEBI, Shareholders.

INTRODUCTION

Corporate governance is concerned with a set of principles, ethics, values, morals, rules, regulations, and procedures, etc, to govern a corporate entity. Corporate governance establishes a system whereby directors are entrusted with duties and responsibilities concerning the direction of the company's affairs. Corporate Governance is a phrase which implies 'transparency of management systems in business and industry, be it the private sector or public sector all of which are corporate entities. It is a set of standards that aims to improve the company's image, efficiency, effectiveness, and social responsibility. The concept of 'corporate governance' is not an end; it's just a beginning towards the long-term growth and prosperity of a company.

Parties to corporate governance

The most influential parties involved in corporate governance include government agencies and authorities

, stock exchanges, management (including the board of directors and its chair, the Chief Executive Officer or the equivalent, other executives and line management, shareholders and auditors). Other influential stakeholders may include lenders, suppliers, employees, shareholders, creditors, customers and the community at large. All parties to corporate governance have an interest, whether direct or indirect, in the financial performance of the corporation. Directors, workers and management receive salaries, benefits and reputation, while investors expect to receive financial returns. For lenders, it is specified interest payments while returns to equity investors arise from dividend distributions or capital gains on their stock. Customers are concerned with the certainty of the provision of goods and services of an appropriate quality; suppliers are concerned with compensation for their goods or services, and possible continued trading relationships. These parties provide value to the corporation in the form of financial, physical, human and other forms of capital. Many parties may also be concerned with corporate social performance.

PRINCIPLES OF CORPORATE GOVERNANCE

According to James D. Wolfensohn, President of the World Bank, "Corporate Governance is about promoting corporate fairness, transparency, and accountability".

The fundamental principles of corporate governance are described below:

Transparency:

Transparency means the quality of something which enables one to understand the truth easily. In the context of corporate governance, it implies an accurate, adequate and timely disclosure of relevant information about the operating results, etc. of the corporate enterprise to the stakeholders.

In fact, transparency is the foundation of corporate governance; which helps to develop a high level of public confidence in the corporate sector. For ensuring transparency in corporate administration, a company should publish relevant information about corporate affairs in leading newspapers, e.g., on a quarterly or half yearly or annual basis.

Accountability:

Accountability is a liability to explain the results of one's decisions taken in the interest of others. In the context of corporate governance, accountability implies the responsibility of the Chairman, the Board of Directors and the chief executive for the use of company's resources (over which they have authority) in the best interest of company and its stakeholders.

Independence:

Good corporate governance requires independence on the part of the top management of the corporation i.e. the Board of Directors must be strong non-partisan body, so that it can take all corporate decisions based on business prudence. Without the top management of the company being independent; good corporate governance is only a mere dream.

OBJECTIVES OF GOOD CORPORATE GOVERNANCE

Good governance is integral to the very existence of the company. It inspires and strengthens investor's confidence by ensuring company's commitment to higher growth and profits. It seeks to achieve the following objectives:

- A properly structured Board capable of taking independent and objective decisions;
- The Board is balanced as regards the representation of adequate number of non-executive and independent directors who will take care of the interests and well being of all shareholders;

- The Board adopts transparent procedures and practices and arrives at decisions on the strength of adequate information;
- The Board has an effective machinery to subserve the concerns of stakeholders;
- The Board keeps the shareholders informed of relevant developments impacting the company;
- The Board effectively and regularly monitors the functioning of the management team;
- The Board remains in control of the affairs of the company at all times.

Therefore, it could be said that overall aim of the Board should be to take the organization forward, to maximize long-term value and shareholder's wealth.

SCOPE OF CORPORATE GOVERNANCE:

The principles of corporate governance cover the following areas :

Rights and equitable treatment of shareholders: Organizations should respect the rights of shareholders and help shareholders to exercise those rights. They can help shareholders exercise their rights by openly and effectively communicating information and by encouraging shareholders to participate in general meetings.

Interests of other stakeholders: Organizations should recognize that they have legal, contractual, social, and market driven obligations to non-shareholder stakeholders, including employees, investors, creditors, suppliers, local communities, customers, and policy makers.

Role and responsibilities of the board: The board needs sufficient relevant skills and understanding to review and challenge management performance. It also needs adequate size and appropriate levels of independence and commitment.

Integrity and ethical behavior: Integrity should be a fundamental requirement in choosing corporate officers and board members. Organizations should develop a code of conduct for their directors and executives that promotes ethical and responsible decision making.

Disclosure and transparency: Organizations should clarify and make publicly known the roles and responsibilities of board and management to provide stakeholders with a level of accountability. They should also implement procedures to independently verify and safeguard the integrity of the company's financial reporting. Disclosure of material matters concerning the organization should be timely and balanced to ensure that all investors have access to clear, factual information.

IMPORTANCE OF CORPORATE GOVERNANCE

A good system of corporate governance is important on account of the following:

Investor Protection: Investors and shareholders of a corporate company need protection for their investment due to lack of adequate standards of financial reporting and accountability. It has been noticed in India that companies raised capital from the market at high valuation of their shares by projecting wrong picture of the company's performance and profitability.

The investors suffered a lot due to unscrupulous management of corporate that performed much less than reported at the time of raising capital. "Bad governance was also exemplified by allotment of promoters' share at preferential prices disproportionate to market value affecting minority holders interest".

Corporate governance is considered as an important means for paying heed to investors' grievances. Kumar Manglam Birla Committee on corporate governance found that companies were not paying adequate attention to the timely dissemination of required information to investors in by India.

Though some measures have been taken by SEBI and RBI but much more required to be taken by the companies themselves to pay heed to the investor's grievances and protection of their investment by adopting good standards of corporate governance.

The importance of good corporate governance lies in the fact that it will enable the corporate firms to

- attract capital and
- perform efficiently.

This will help in winning investors' confidence. Investors will be willing to invest in the companies with a good record of corporate governance.

New policy of liberalization and deregulation adopted in India since 1991 has given greater freedom to management which should be prudently used to promote investors' interests. In India there are several instances of corporate' failures due to lack of transparency and disclosures and instances of falsification of accounts. This discourages investors to make investments in the companies with poor record of corporate governance.

Global Perspective. The extent to which corporate enterprises observe the basic principles of good corporate governance has now become an important factor for attracting foreign investment. In this age of globalisation when quantitative restrictions have been removed and trade barriers dismantled, the relationship between corporate governance and flows of foreign investment has become increasingly important.

Studies in India and abroad show that foreign investors take notice of well- managed companies and respond positively to them, capital flows from foreign institutional investors (FII) for investment in the capital market and foreign direct investment (FDI) in joint ventures with Indian corporate companies will be coming if they are convinced about the implementation of basic principles of good corporate governance.

Thus, "International flows of capital enable companies to access financing from a large pool of investors. If countries are to reap the full benefits of the global capital markets, and if they are to attract long-term capital, corporate governance arrangements must be credible and well understood across borders". The large inflows of foreign investment will contribute immensely to economic growth.

Indispensable for healthy and vibrant stock market. An important advantage of strong corporate governance is that it is indispensable for a vibrant stock market. A healthy stock market is an important instrument for investors protection. A bane of stock market is insider trading. Insider trading means trading of shares of a company by insiders such directors, managers and other employees of the company on the basis of information which is not known to outsiders of the company.

It is through insider trading that the officials of a corporate company take undue advantage at the expense of investors in general. Insider trading is a kind of fraud committed by the officials of the company. One way of dealing with the problem of insider trading is enacting legislation prohibiting such trading and enforcing criminal action against violators.

NEED FOR CORPORATE GOVERNANCE

The need for corporate governance is highlighted by the following factors:

Wide Spread of Shareholders:

Today a company has a very large number of shareholders spread all over the nation and even the world; and a majority of shareholders being unorganised and having an indifferent attitude towards corporate affairs. The idea of shareholders' democracy remains confined only to the law and the Articles of

Association; which requires a practical implementation through a code of conduct of corporate governance.

Changing Ownership Structure:

The pattern of corporate ownership has changed considerably, in the present-day-times; with institutional investors (foreign as well Indian) and mutual funds becoming largest shareholders in large corporate private sector. These investors have become the greatest challenge to corporate managements, forcing the latter to abide by some established code of corporate governance to build up its image in society.

Corporate Scams or Scandals:

Corporate scams (or frauds) in the recent years of the past have shaken public confidence in corporate management. The event of Harshad Mehta scandal, which is perhaps, one biggest scandal, is in the heart and mind of all, connected with corporate shareholding or otherwise being educated and socially conscious.

The need for corporate governance is, then, imperative for reviving investors' confidence in the corporate sector towards the economic development of society.

Greater Expectations of Society of the Corporate Sector:

Society of today holds greater expectations of the corporate sector in terms of reasonable price, better quality, pollution control, best utilisation of resources etc. To meet social expectations, there is a need for a code of corporate governance, for the best management of company in economic and social terms.

Hostile Take-Overs:

Hostile take-overs of corporations witnessed in several countries, put a question mark on the efficiency of managements of take-over companies. This factors also points out to the need for corporate governance, in the form of an efficient code of conduct for corporate managements.

Huge Increase in Top Management Compensation:

It has been observed in both developing and developed economies that there has been a great increase in the monetary payments (compensation) packages of top level corporate executives. There is no justification for exorbitant payments to top ranking managers, out of corporate funds, which are a property of shareholders and society.

This factor necessitates corporate governance to contain the ill-practices of top managements of companies.

Globalisation:

Desire of more and more Indian companies to get listed on international stock exchanges also focuses on a need for corporate governance. In fact, corporate governance has become a buzzword in the corporate sector. There is no doubt that international capital market recognises only companies well-managed according to standard codes of corporate governance.

KEY ISSUES IN CORPORATE GOVERNANCE IN INDIA – MANAGING THE DOMINANT SHAREHOLDER(S) AND THE PROMOTER(S)

The primary difference between corporate governance enforcement problems in India and most western economies (on whose codes the Indian code is largely modeled) is that the entire corporate governance approach hinges on disciplining the management and making them more accountable. The 'agency gap' in western economies represents the gap between the interests of management and dispersed shareholders and corporate governance norms are aimed at reducing this gap. However, in India the problem—since the inception of joint-stock companies—is the stranglehold of the dominant or principal shareholder(s) who monopolize the majority of the company's resources to serve their own needs. That is, the 'agency gap' is actually between majority shareholders and other stakeholders.

Secondly, much of global corporate governance norms focus on boards and their committees, independent directors and managing CEO succession. In the Indian business culture, boards are not as empowered as in several western economies and since the board is subordinate to the shareholders, the will of the majority shareholders prevails.

Therefore, most corporate governance abuses in India arise due to conflict between the majority and minority shareholders. This applies across the spectrum of Indian companies with dominant shareholders—PSUs (with government as the dominant shareholder), multinational companies (where the parent company is the dominant shareholder) and private sector family-owned companies and business groups.

Public Sector Units

In public sector units (PSUs), members of the board and the Chairman are usually appointed by the concerned ministry and very often PSUs are led by bureaucrats rather than professional managers. Several strategic decisions are taken at a ministerial level which may include political considerations of business decisions as well. Therefore, PSU boards can rarely act in the manner of an empowered board as envisaged in corporate governance codes. This makes several provisions of corporate governance codes merely a compliance exercise.

Multinational companies

Multinational companies (MNCs) in India are perceived to have a better record of corporate governance compliance in its prescribed form. However, in the ultimate analysis, it is the writ of the large shareholder (the parent company) which runs the Indian unit that holds sway, even if it is at variance with the wishes of the minority shareholders. Moreover, the compliance and other functions in an MNC are always geared towards laws applicable to the parent company and compliance with local laws is usually left to the managers of the subsidiary who may not be empowered for such a role.

Family businesses

Family businesses and business groups as a category are perhaps the most complex for analysing corporate governance abuses that take place. The position as regards family domination of Indian businesses has not changed; on the contrary, over the years, families have become progressively more entrenched in the Indian business milieu.

As per a recent study the global financial major credit suisse, India ranks higher than most Asian economies in terms of the number of family businesses and the market capitalization of Indian family businesses as a share of nominal gross domestic product(GDP) has risen from 9 percent in 2001 to 46 percent in 2010.

This survey, which also covered China, South Korea, Taiwan, Singapore, Thailand, Hongkong, Indonesia, Malasiya and phillipines, contends that India, with a 67% of family businesses, ranks first amongst ten Asian countries studied. Furthermore, 663 of the 983 listed Indian companies are family businesses and account for half of the total corporate hiring and are concentrated in the consumer discretionary, consumer staples and consumer health care sectors.

CORPORATE GOVERNANCE ISSUES BASED ON DIFFERENT TYPES OF OWNERSHIP AND MANAGEMENT

For the purpose of this section, we define five categories of companies based on their pattern of ownership and management:

- **Promoter-managed companies:** Companies where the top executive (whether MD/CEO or executive chairman) is a representative of the promoter-family e.g.: Reliance Industries, Bajaj Auto.
- **Promoter-owned, Professionally managed companies**: Companies where ownership and management is separated, where the MD/CEO is a professional, while the promoter family representative holds only a seat on the company's board e.g: Tata Group, Mahindra group
- **Foreign owned companies:** Companies which are the Indian subsidiaries of foreign multinational corporations e.g.: HUL, Nestle, Bosch India etc
- **PSUs**: Public Sector Undertakings -companies where the government is a major shareholder.
- **Institutionally owned and managed companies:** Companies where the ownership is widely dispersed and no family or foreign shareholder or institution has a majority stake e.g.: ITC, HDFC, ICICI Bank, L&T etc.

The central problem in Indian corporate governance is not a conflict between management and owners as in the US and the UK, but a conflict between the dominant shareholders and the minority shareholders. The problem of the dominant shareholder arises in three large categories of Indian companies. First are the public sector units (PSUs) where the government is the dominant (in fact, majority) shareholder and the general public holds a minority stake. Second are the multinational companies (MNCs) where the foreign parent is the dominant (in most cases, majority) shareholder. Third are the Indian business groups where the promoters (together with their friends and relatives) are the dominant shareholders with large minority stakes, government owned financial institutions hold a comparable stake, and the balance is held by the general public. It is important to bear in mind that the relation between the company and its shareholders and the relation between the shareholders inter-se is primarily contractual in nature.

CORPORATE GOVERNANCE: THE NEED FOR REGULATION

There are at least three reasons for regulatory intervention.

- The main reason advocated in favour of mandatory rules is that, if the founder of the company was allowed to design and implement a corporate charter he likes, he may not clearly address the issues faced by other shareholders and thus would, in the view of the society, conjure inefficient rules. In absence of regulations, founders could employ anti-takeover defenses excessively and in the process not allow the capital employed, which is owned by the shareholders, to be used most efficiently.
- Another argument for mandating regulations of corporate governance comes from the externality argument. An externality may be defined as a good, generated as the result of an economic activity, whose benefits or costs do not accrue directly to the parties involved in the activity. .One corporate failure or scandal can potentially erode shareholders trust in the whole of the corporate sector and thus negatively affect the businesses of honest firms as well.
- The final argument in support of mandatory rules is to avoid a situation where efficient rules are designed initially but due to lack of active tracking by dispersed shareholders, are altered or broken later.

CORPORATE GOVERNANCE INITIATIVES IN INDIA

In India, the initiative on corporate governance was not a result of any major corporate scandal, like Enron, World Com, etc. It started as a self-regulatory move from the industry rather than the rule of law. The very first formal corporate governance initiative in India came from an industry association in 1998 and was voluntary in nature. Over the next few years, corporate governance as a concept has gained in importance and has seen many studies, task forces and even legislation. The corporate governance system in India is a hybrid of the arms-length market-based system of UK and USA and the insider-dominated bank-based systems of Germany and France.

The CII Code

Confederation of Indian Industries (CII) set up a task force in 1995 under Rahul Bajaj, a reputed industrialist. It's object was to develop and promote a code for corporate governance to be adopted and followed by Indian companies. The committee was driven by the conviction that good corporate governance was essential for Indian companies to access domestic as well as global capital at competitive rates. The first draft of the code was prepared by April 1997, and the final document (Desirable Corporate Governance: A Code), was publicly released in April 1998. The code was voluntary, contained detailed provisions, and focused on listed companies.

Kumar Mangalam Birla committee report and Clause 49 Of Listing agreement

While the CII code was well-received and some progressive companies adopted it, it was felt that under Indian conditions a statutory rather than a voluntary code would be more purposeful, and meaningful.
Consequently, the second major corporate governance initiative in the country was undertaken by SEBI. In early 1999, it set up a committee under Kumar Mangalam Birla to promote and raise the standards of good corporate governance. In early 2000, the SEBI board had accepted and ratified key recommendations of this committee, and these were incorporated into Clause 49 of the Listing Agreement of the Stock Exchanges.

The Naresh Chandra committee report on corporate governance

The Naresh Chandra committee was appointed in August 2002 by the Department of Company Affairs (DCA) under the Ministry of Finance and Company Affairs to examine various corporate governance issues. The Committee submitted its report in December 2002. It made recommendations in two key aspects of corporate governance: financial and non-financial disclosures and independent auditing and board oversight of management.

Narayana Murthy committee report on corporate governance

The fourth initiative on corporate governance in India is in the form of the recommendations of the Narayana Murthy committee. The committee was set up by SEBI, under the chairmanship of Mr. N. R. Narayana Murthy, to review Clause 49, and suggest measures to improve corporate governance standards. Some of the major recommendations of the committee primarily related to audit committees, audit reports, independent directors, related party transactions, risk management, directorships and director compensation, codes of conduct and financial disclosures.

LEGAL FRAMEWORK OF CORPORATE GOVERNANCE IN INDIA:

The corporate governance framework in India primarily consists of the following legislations and regulations:

CORPORATE GOVERNANCE IN COMPANIES ACT, 2013

The Companies Act was enacted on August 30, 2013 which provides for major overhaul of corporate governance norms for all companies. One of the important areas of corporate governance introduced in Companies Act, 2013 has been introduction of :

- **Independent Director**
  Under the Companies Act, 2013 the strength of number of Independent directors for the prescribed companies under Section 149(4) read with Rule 4 of Companies (Appointment and Qualifications of Directors) Rules, 2014 is as follows:
- **Woman Director**
  Section 149 (1) of the Companies Act, 2013 prescribes the following classes of companies to have at least one woman director.
- All listed companies
- Non-listed public companies having paid up share capital of Rs.100 crores or more or having turnover of Rs.300 crores or more
- Section 134

Section 134 provides that a report by the Board of Directors containing details on the matters specified including directors responsibility statement shall be attached to every financial statement laid before a company. The responsibility statement includes that the applicable Accounting Standards have been followed in preparing the financial statements and reporting the material departures therefrom, that the companies follow their accounting policies consistently, the accounts have been prepared on a going concern basis and compliance of all applicable laws.

- **Audit Committees (section 177)**

The Companies Act,2013 has increased the ambit of companies to constitute audit committees. Section 177 provides the requirements and manner of constituting the Audit Committee. The Audit Committee shall consist of minimum three directors with Independent Directors forming a majority and majority members must have ability to read and understand financial statements. The Section also provides for a vigil mechanism in every listed and prescribed class of companies and such mechanism shall be disclosed at the website of the company and should be mentioned in Board's report.

It shall be applicable to all the listed companies or non-listed public companies having paid up share capital of Rs.10 crores or more, Turnover of Rs.100 crores or more, aggregate outstanding loan of Rs. 50 crores or more.

- **Composition of Nomination & Remuneration Committee& Stakeholder relationship Committee**

Section 178(1) of the Companies Act prescribes appointment of Nomination and Remuneration committee. The duty of the Committee shall be to identify the persons who are qualified to become directors and who can be appointed in the senior management and carry out the evaluation of directors. Section 178(5) prescribed appointment of stakeholder relationship Committee to resolve grievances of security holders of company.

The Nomination and Remuneration Committee is applicable to the following classes of Companies-

- Every listed Company
- Every other Public company-
  - Having **Paid up capital of Rs.100 crores or more**; or
  - Which have, in aggregate, outstanding **loans or borrowings or debentures or deposits exceeding Rs.50 Crores.**
- **Internal Audit**

Companies Act, 2013 has mandated the internal audit for certain classes of companies under Section 138.

These companies includes all the listed companies, All listed companies having paid up share capital of Rs. 50 crores or more, all the non-listed companies having paid up share capital of Rs.50 crores or more, turnover of Rs.200 crores or more in the preceding financial year, outstanding loans or borrowings from the banks or public financial institutions of Rs.100 crores or more.

- **Serious Fraud Investigation Office (SFIO)**

Section 211 (1) of the Companies Act, 2013 shall establish an office called the Serious Fraud Investigation office to investigate fraud relating to Company. SFIO can investigate into the affairs of the company or on receipt of report of Registrar or inspector or in the public interest or request from any Department of Central Government or State Government.

- **Corporate Social Responsibility**

Section 135(1) of Companies Act, 2013 prescribes that every company shall constitute Corporate Social Responsibility Committee constituting of three or more directors with at least one independent director. These companies includes companies having net worth of Rs. 500 crores or more, turnover of Rs.1000 crore or more, or net profit of Rs.5 crores or more during any financial year.

CORPORATE GOVERNANCE UNDER SEBI

SEBI, being the securities market regulator in India has primary oversight on investor protection and its establishment played a significant role in establishing norms for the corporate governance in India. The SEBI Act, 1992 ("**SEBI Act**") empowers SEBI to frame regulations, pursuant to which the regulator has introduced a comprehensive set of guidelines on insider trading, mergers and takeovers, fraudulent practices, etc all of which have a significant impact on corporate governance in the country.

SEBI, as a market regulator, also decides the terms and conditions of listing agreement which govern the arrangement between stock exchanges and companies listed on the stock exchange. The listing agreement usually requires disclosures to be made by the company to the stock exchange. For instance, in terms of Clause 41 of the listing agreement, a company is required to submit quarterly financial results to the recognized stock exchange and these results are required to be approved by the Board of a company or by a committee (other than the audit committee).

While doing this, the Chief Executive Officer and Chief Financial Officer of the company, (by whatever name called), is required to certify that the financial results do not contain any 'false or misleading statement or figures and do not omit any material fact which may make the statements or figures contained therein misleading.' The corporate governance standards are elaborated in Clause 49 of the listing agreement. However, this agreement was codified in the year 2015 by the enactment of SEBI (Listing Obligations and Disclosure Requirements).

SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations)

On September 2, 2015, SEBI notified the Listing Obligations and Disclosure Requirements Regulations, 2015 ("**2015 Regulations**") with **two-fold objectives:**

- firstly, to align clauses of the listing agreement with Companies Act and
- secondly, to consolidate the conditions under different securities' listing agreements in one single regulation.

The 2015 Regulations are **applicable to** any entity (whether a company or not) accessing the stock exchange, for listing equity shares (on main board, SME exchange, institutional trading platforms), debt securities, preference shares, depository receipts, securitized debt instruments, mutual fund units, and other securities as may be specified by SEBI.

The regulations as to corporate governance are discussed there under:

1. Stricter governance requirements on board of directors

The 2015 Regulations in certain instances moves beyond mere alignment with governance requirements and thresholds as provided under the Companies Act and adopts a stricter approach towards the composition of board, its committees and the duties of directors. It tends to retain the higher requirements of Clause 49 of the equity listing agreement as well as amends some of the voluntary guidelines, to make them mandatory.

- **Board composition and its committees:**

For instance, as per Companies Act, at least 1/3rd of the board of directors of a listed company must comprise of independent directors. However, Regulation 17 retains the earlier threshold requiring 50% of the board to be independent, if the chairperson is not a non-executive director.

Similarly, while the Companies Act requires that the audit committee members must be financially literate (i.e. capable of reading and understanding financial statements), Regulation 18(1)(c) maintains the mandate of having at least 1 member who possesses "accounting or related financial management expertise".

Further, it also retains the requirement of valid quorum of at least 2 independent directors for conducting an audit committee meeting, thereby making it indirectly imperative for all listed companies to appoint at least 2 independent directors.

The 2015 Regulations also provide for constitution of "risk management committee" for top 100 listed entities determined on the basis of market capitalization at the end of previous financial year. Earlier, the listing agreement merely mandated the board to inform the shareholders regarding risk assessment and minimization procedures adopted for the same without requirement of a specific committee as such.

Furthermore, constitution of remuneration committee and framing of whistleblower policy are now made mandatory compliances as opposed to voluntary practice under the listing agreement. Additionally, Regulation 46 requires disclosure of composition of various board committees on company's website.

- **Duties of the board:**

Section 166 of the Companies Act codifies the fiduciary duties of directors and breach of the duties is punishable with fine between INR 100,000 (about US$ 1,500) to INR 500,000 (about US$ 7,700).

The 2015 Regulations further elaborate these codified duties, and provide principle-based guidelines in Regulation. These principles impose a collective duty on the board of directors for ensuring good governance. For instance, it is mandated that the board must disclose any matter that directly affects the company;

1. conduct itself so as to meet expectations of operational transparency while maintaining confidentiality;
2. monitor effectiveness of governance practices;
3. align managerial remuneration with long term interests of the company and the shareholders;
4. ensure transparent nomination;
5. monitor and manage conflict of interest;
6. ensure integrity of accounting and financial reporting systems; etc.

These principles are subjective and whether the duty has been fulfilled or not will be determined on a case-to-case basis. Further, it is expressly provided that in case of any ambiguity or inconsistency between the principles and the specific regulations, the principles shall prevail. It is unclear at this stage as to how will listed companies' boards ensure collective compliance with these ideologies and whether breach by any individual will result in impugning liability on the entire board as officer-in-default.

2. Related Party Transactions

Related party transactions ("**RPTs**") continue to garner constant attention for Indian companies. The Companies Act initially mandated special resolution for specific RPTs exceeding prescribed threshold. The Ministry of Corporate Affairs through an amendment in 2015 replaced the requirement of special resolution by an ordinary resolution. It also issued a circular clarifying that only such related parties who are related to the particular transaction should abstain from voting on the proposed resolution. One of the objectives for notifying the 2015 Regulations was to streamline the process of RPT approval for listed companies in light of these changes.

3. Scope of RPTs:

The 2015 Regulations defines RPT as **'transfer of resources, services or obligations between a listed entity and a related party, regardless of whether a price is charged'**.

Further, "transaction" must be interpreted to include a single or a group of transactions under a particular contract. This definition is wider in scope than the Companies Act.

As per Section 188 of the Companies Act,2013 a transaction with related party is not an RPT and does not require prior board or shareholders' approval as long as it is at an "arm's-length" basis occurring in the "ordinary course of business". In light of the scope of RPTs under the 2015 Regulations, the exemption is taken away irrespective of the size of the listed entity and the value of the transaction in question. Hence, any transaction which is a RPT will require not only prior audit committee approval as mandated under Regulation 23(2), but also require board approval. However, shareholders' approval will be only necessitated if the transaction is a material RPT.

4. Approval of RPTs:

Regulation 23(1) requires every listed entity to formulate a policy on materiality of RPTs. It also provides that any transaction with a particular related party (taken individually or combined with other transactions during the financial year) which exceeds 10% of listed company's annual consolidated turnover shall be considered a material RPT. It appears that a listed company may determine the variety of RPTs which will be classified as material ones. Since such materiality cannot transgress the threshold prescribed under the Companies Act; companies must take them into consideration while framing the policy on material RPTs.

In order to align with the recent amendment in Companies Act, the 2015 Regulations substitute the old mandate of approving RPTs through special resolution, thereby permitting listed entities to approve RPTs through an ordinary resolution. But, the restriction on voting by related parties is not done away with, despite the clarification issued by the Ministry of Corporate Affairs which allows non-interested related parties to vote for approving a particular RPT.

Regulation 23(4) read along with 23(7) states that while approving material RPTs, all related parties whether or not concerned with the particular RPT, must abstain from exercising their votes. Therefore, the RPTs approval process under the 2015 Regulations take away major exceptions and overall continue to remain stricter in comparison to the Companies Act.

5. Corporate governance for listed start-ups

In August 2015, SEBI amended the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 to enable listing of certain categories of start-ups without undergoing an initial public offer. The underlying objective was to liberalize the stricter listing compliances and disincentivize start-ups opting to list on foreign stock exchanges. These start-ups must alter their structure into public companies prior to listing.

Further, they can raise capital only through rights issue and private placement (which were otherwise available under Companies Act) and cannot invite retail investments or make any public offer. SEBI's model agreement for listing on the institutional trading platform did not relax the start-ups from complying with the corporate governance requirements as contained in the Companies Act. For instance, a listed start-up has to necessarily appoint 1/3rd of its board with independent directors, appoint 1 woman director, constitute board committees, set up vigil mechanism and put in place various internal controls and systems. Compliance with corporate governance provisions involves structural and compliance costs, substantial time for a start-up and continues to act as a deterrent for listing, despite floating of the alternative mechanism.

In order to exempt start-ups from such governance requirements, the 2015 Regulations seem to make a failed attempt. Regulation 15(2) exempts compliance with corporate governance practices for (i) companies with paid-up equity capital below INR 100 million (about US$ 1.5 million) and net worth less than INR 250 million (about US$ 3.9 million), and (ii) companies listed on SME exchanges. However, effect of such exemption is nullified by Regulation 15(3) which states that provisions of Companies Act shall apply where they are triggered. Thus, a listed start-up will continue to be governed by similar corporate governance parameters as that of a listed public company, even though it does not raise funds through a public offer.

Contravention of the 2015 Regulations will result in imposition of fines, suspension of trading, freezing of promoter or promoter group shares, or any other action as SEBI may deem fit. Further, the 2015 Regulations give statutory status to the contractual clauses of listing agreements and thus, breach of the 2015 Regulations will invoke penalty clauses under the SEBI Act.

GOVERNMENTAL INITIATIVES – MEASURES BY MCA

MCA is the executive arm which regulates the functioning of the corporate sector. It primarily administers the Companies Act and other allied acts, such as the Competition Act, 2002, Partnership Act, 1932, Companies (Donations to National Funds) Act, 1951 and Societies Registration Act, 1860. The MCA also exercises supervision over three separate bodies, established by the Parliament, concerned with the professions of Chartered Accountants, Company Secretaries and Cost Accountants respectively. As the primary government body, MCA has taken a number of steps in establishing the standards for corporate governance in the country. Some of the key initiatives taken by MCA are highlighted below:

1. Voluntary Guidelines on Corporate Governance

MCA introduced the Voluntary Guidelines on Corporate Governance in 2009 ("Guidelines"), a set of best practices to develop ethical and responsible standards in the Indian industry. The Guidelines are completely voluntary in nature but are strongly recommended by the government to all public companies and large private companies as well. The guidelines relate to various issues such as: the constitution of Board (appointment, role of independent directors, remuneration); the responsibilities of the Board (training, enabling quality decision making, risk management, evaluation of performance, compliance); audit committees of Board (constitution, enabling powers, role and responsibilities); and auditors (appointment, certificate of independence, rotation); secretarial audit; whistle blowers, etc.

2. Green Initiatives

A number of green initiatives have also been recently introduced, such as: (i) service of documents through electronic mode to increase the speed of delivery, (ii) participation of directors and shareholders through video conferencing to provide larger participation and for curbing the cost borne to attend various meeting

, (iii) secure electronic voting in the general meetings of the company and (iv) issuance of digital certificates and standard letters by the Registrar of Companies ("ROCs") to reduce the delay.

3. Serious Fraud Investigation Office ("SFIO")

In 2003, SFIO was set up in the backdrop of stock market scams, failure of non financial banking companies, phenomena of vanishing companies and plantation companies. The office investigates cases which have inter-departmental and multi-disciplinary ramifications or public interest at stake or the possibility of investigation contributing towards an improvement in systems, laws or procedures. The investigation is carried out only when it has been referred by the Central Government under section 235 and 237 of the Companies Act.

4. Investor Grievances Management Cell ("IGMC")

IGMC, earlier known as the Investor Protection Cell, was set up by the MCA in 1993 with the objective of resolving the grievances of investors' through the jurisdictional ROCs. IGMC coordinates with the RBI, SEBI and Department of Economic Affairs and broadly, deals with issues like non receipt of annual report, non receipt of dividend amount, non refund of application money, etc. Recently, MCA has also permitted the use of MCA-21, an online portal, to receive grievances online.

5. National Foundation for Corporate Governance ("NFCG")

NFCG, the national apex platform on corporate governance issues, was established in 2003 by the MCA to act as a platform for deliberation on issues relating to corporate governance and to sensitize corporate leaders on the importance of "good corporate governance, self-regulation and directorial responsibilities". Along with MCA, the other stakeholders in NFCG are: Confederation of Indian Industry, Institute of Chartered Accountants of India, Institute of Company Secretaries of India, Institute of Cost and Works Accountants of India, and National Stock Exchange of India Limited.

CONCLUSION

Corporate governance has emerged as a cornerstone of effective business management in the contemporary corporate landscape. It is not merely a set of rules or guidelines but a comprehensive system that ensures companies are directed and controlled in a responsible, transparent, and accountable manner. This paper has emphasized that corporate governance involves the processes by which corporate objectives are formulated and pursued within the broader context of social, legal, and market environments. These processes serve to align the interests of management with those of stakeholders, ensuring that the company's operations are carried out in a manner that promotes sustainability, ethical conduct, and long-term value creation.

A well-structured corporate governance system is essential for maintaining stakeholder confidence. It ensures that companies are not only focused on profit maximization but are also committed to ethical decision-making and responsible corporate behavior. By promoting transparency, fairness, and accountability, good governance practices build trust among investors, employees, customers, regulators, and the broader community. This trust, in turn, becomes a crucial asset for companies striving to remain competitive and resilient in today's dynamic business environment.

Moreover, good governance contributes significantly to improving the quality of decisions made by those in leadership roles. Ethical decision-making supported by a robust governance framework helps organizations anticipate and manage risks more effectively, enhances operational efficiency, and fosters innovation. In the long term, these elements collectively contribute to the sustainability and profitability of the business. Therefore, corporate governance is not simply a regulatory requirement—it is a strategic necessity for any organization that seeks to succeed and grow responsibly.

Recommendations:

1. **Establish a Robust Governance Framework**

Organizations should implement a comprehensive governance structure that clearly defines the roles, responsibilities, and authority of the board of directors, executive management, and other key stakeholders. A well-defined governance framework ensures that decision-making processes are streamlined, responsibilities are clearly allocated, and accountability mechanisms are in place.

2. **Foster a Culture of Ethical Leadership**

Ethical behaviour must be embedded at every level of the organization, beginning with top leadership. Companies should promote a values-driven culture where integrity, honesty, and transparency are prioritized. Ethical leadership not only sets a positive example for employees but also reinforces the company's reputation and stakeholder trust.

3. **Enhance Stakeholder Communication and Engagement:**

Effective corporate governance requires ongoing dialogue with stakeholders. Companies should establish regular, transparent communication channels to share relevant information about financial performance, strategic plans, risks, and governance practices. Actively engaging stakeholders enables companies to better understand and address their concerns, leading to more informed and inclusive decision-making.

4. **Invest in Board Training and Development:**

Continuous professional development for board members is essential to ensure they are well-equipped to fulfill their governance responsibilities. Companies should provide training on evolving legal and regulatory frameworks, emerging industry trends, ethical standards, and risk management practices. An informed and skilled board is better positioned to make sound strategic decisions.

5. **Implement Effective Monitoring and Evaluation Mechanisms**

Regular internal and external audits, risk assessments, and performance evaluations should be part of the governance process. These mechanisms help identify potential weaknesses, ensure compliance with legal requirements, and promote continuous improvement in governance practices. Monitoring systems must be objective, comprehensive, and supported by reliable data.

6. **Leverage Technology for Governance Efficiency**

In an increasingly digital world, technology can be a powerful enabler of good governance. Companies should utilize digital tools and platforms for real-time data analysis, risk monitoring, compliance tracking, and reporting. Automation and data-driven insights can significantly improve decision-making efficiency and ensure timely interventions when governance issues arise.

7. **Adapt to Evolving Regulatory and Market Demands**

Governance systems must be dynamic and responsive to changes in the legal, economic, and technological environments. Organizations should periodically review and update their governance policies to remain compliant and competitive. Flexibility and adaptability are key to maintaining effective governance in a rapidly changing world.

In conclusion, strong corporate governance is indispensable for fostering ethical conduct, enhancing stakeholder confidence, and building sustainable, high-performing businesses. Companies that invest in effective governance systems are better positioned to manage risks, capitalize on opportunities, and deliver long-term value for all stakeholders.

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