ROLE OF CORPORATE GOVERNANCE IN INDIA: THE ORGANIZATIONAL DIMENSION OVER YEARS AND ITS FUTURE

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Abstract

Corporate governance, in its essence, is a system of applying best management practices by stressing on ethical and socially responsible standards which will improve the sustainable relationship between all the stakeholders of a Company. Anchoring upon its pillars of strength viz. transparency, accountability, fairness and ethics, corporate governance put forward a valid and righteous governance for the corporates.

When the pathway of corporate governance is explored, it is tacit that, 'corporate governance' is not a new concept, but only a new phrase. History shows that whenever there occurred an instance of demarcation of owners with managers, there felt a need for corporate governance, in its meaning as we conceptualize now. Shakespeare, in his notable work '***Merchant of Venice***' marked such an instance where Antonio had to endure the pain of seeing his sail going away from him with his fortunes in the hands of others. In the Indian context too, the concept was addressed in '***Arthashastra***' by Chanakya, where the Kings faced from their royal officials the roots of mismanagement. The need for governance was always needed and felt, only that it became realized in the form of 'Corporate governance' in 1960s. The Cadbury Committee (1992) report defined the corporate governance exactly as is practiced now.

As far as Indian context is considered, the evolution of corporate governance can be traced in three phases. The first phase marked 'Managing Agency

System', followed by 'Promotor system' and finally the 'corporate governance' phase as defined by ICAI. The Harshad Mehta scam of 1992 paved way for strengthening the core principles of corporate governance in India. Actually, it can be said that the concept is reinforcing more and more year after year. And of course, the insights from the Satyam scam (2009), Sarada Chit fund scam (2013) and PACL scam (2015) contributed to it considerably. When we look at the various organizational dimension of corporate governance in India, remarkable inferences can be drawn, for instance, from banking sector, small and medium enterprises, public enterprises, financial sector enterprises, energy sector enterprises, etc. Moreover, it is interesting to find E-governance as a new dimension in India along with the role of 'Gender diversity' in corporate governance and its impact on the corporate performance.

Keywords: Corporate Governance, Gender diversity, E-governance, Managing Agency System.

I. INTRODUCTION TO CORPORATE GOVERNANCE

Corporate governance, in its essence, is a system of applying best management practices by stressing on ethical and socially responsible standards which will improve the sustainable relationship between all the stakeholders of a Company. Anchoring upon its pillars of strength viz. transparency, accountability, fairness and ethics, corporate governance puts forward a valid and righteous governance for the corporates.

The term, 'corporate governance' itself tells the meaning that, it is an act of governing/ managing corporates. The need for governance arises because of its basic structure. As it is a known fact that equity capital is the fundamental and inevitable source for any company, the company will have to raise equity capital that will be divided into a number of shares thus resulting in having numerous shareholders for a company. It is impossible for each of them to get involved into the daily activities of the company. Therefore, it is obvious that their representatives and managers run the business. When such a system exists, there arise conflict in the interests. History reveals that the management often fails to keep the interests of shareholders. Malpractices and window dressing began to increase more and more. The world witnessed the dark side of corporate mismanagement through various scams across nations. It was then the need for prompt solution to the issue stimulated. And the solution was 'Corporate Governance'.

Corporate governance addresses the very fundamental issue of the corporates – the separation of owners and management. As there is a separation between shareholders, who are the owners, and the management, who manages the companies on behalf of the owners, there arise a need for governance. Corporate governance lays down a set of principles and guidelines in which the corporates need to work by protecting the interests of shareholders. It also makes ensure that the corporates fully understand and imbibe the fact that they are accountable to all its stakeholders including shareholders, employees, customers, creditors, government and the public.

The term governance is derived from the Latin word 'gubernate' meaning 'to steer' and the term 'corporate' from the Latin word 'corpus' meaning a 'body'. Thus corporate governance is aimed at steering the corporates towards the desired direction. It lays down a set of principles, procedures, process, systems and standards to ensure transparency and honesty in the functioning of corporates. It stresses on identifying and sticking upon the integrity and identity of an organization and giving right prominence to ethics and fiduciary relationship with stakeholders. That is, corporate governance is all about the way in which a corporate is managed and directed. The board of directors should direct the corporate in such a way as to achieve shareholders' and other stakeholders' interest, not their own personal interests. The board will be automatically benefited when the stakeholders are benefitted and the company is grown. Thus, a balancing of individual and social goals is aimed through corporate governance. That is, both economic and social goals are met judiciously.

Another salient aspect of corporate governance is that it gives complete and ultimate authority and responsibility to the Board of Directors. Their interactions with the other stakeholders of the company and maintaining a health relations have significant role in shaping the company and its performance. It is their duty to not to make any grounds for conflicts. The functions of managers and owners should be clearly distinguished and all the

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functions to be harmonized. Ultimately, corporate governance envisages added value to its stakeholders by promoting ethical, moral and trustworthy practices.

According to Cadbury Committee (1992), **"Corporate governance is the system by which companies are directed and controlled. It encompasses the entire mechanics of the functioning of a company and attempts to put in place a system of checks and balances between the shareholders, directors, employees, auditor and the management.** (Governance, n.d.)**"** The Institute of Company Secretaries of India defines corporate governance as **"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 sustainable development of all stakeholders"**.

II. HISTORY/EVOLUTION

When the pathway of corporate governance is explored, it is tacit that, 'corporate governance' is not a new concept, but only a new phrase. History shows that whenever there occurred an instance of demarcation of owners with managers, there felt a need for corporate governance, in its meaning as we conceptualize now. Shakespeare, in his notable work '***Merchant of Venice***' marked such an instance where Antonio had to endure the pain of seeing his sail going away from him with his fortunes in the hands of others. In the Indian context too, the concept was addressed in '***Arthashastra***' by Chanakya, where the Kings faced from their royal officials the roots of mismanagement. The need for governance was always needed and felt, only that it became realized in the form of 'Corporate governance' in 1960s. The Cadbury Committee (1992) report defined the corporate governance exactly as is practiced now.

The 17th century marked the growth of trade and monopolists in the world history. Economic powers like Britain, Holland, Portugal and Germany made their own empire. The East India Company, which was a joint stock company began in that century. The famous economist Adam Smith, in 1776 noted the root cause of corporate governance: **"The directors of Companies, being the managers of other people's money rather than their own, cannot well be expected to watch over it with the same anxious vigilance with which (they) watch over their own".**

The 19th century saw the growth of limited liability companies and the resultant huge industrial growth. However, as the companies grew and grew, and the geographical width of shareholders as well grew, the problems of mismanagement began. The 20th century witnessed the development in management thoughts and theories. It is 21st century which can be said as the era of corporate governance. Many emerging and developed economies began to introduce corporate governance codes in their respective nations. The nations that adopted corporate governance at an early stage with distinctive characteristics are Canada, US, UK, Italy, France, Germany, Japan, China and India.

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'Promotor system' and finally the 'corporate governance' phase as defined by ICAI. The Harshad Mehta scam of 1992 paved way for strengthening the core principles of corporate governance in India. Actually, it can be said that the concept is reinforcing more and more year after year. And of course, the insights from the Satyam scam (2009), Sarada Chit fund scam (2013) and PACL scam (2015) contributed to it considerably.

IV. SCAMS AND FRAUDS

The rising of corporate frauds and scams led to the need for corporate governance all over the world. The major scams that shook the world include Enron debacle, WorldCom fraud, AIG insurance case, Barings bank case, Lehman Brother case, Satyam case, Tata finance case and Sahara Pariwar case.

The Enron, the US Energy, Commodities and Services Company was founded in 1985 and had a good rise in the market for decades. The downfall of the company was marked on 2001 when they used dubious accounting practices to cover up their problems through "mark-to-market accounting". The WorldCom scandal (2002) was revealed when the US's second largest telecommunications company admitted they have overstated its earnings to show inflated profits to cover up the loss of around 3.8 billion dollars[1]. The American International Group (AIG) made a big collapse during the subprime crisis due to its wide issuance of insurance contracts without analyzing risk involved in it. The great fall of Barings bank (a 233 year old bank) happened in 1995 when one of its traders Nick Leeson lost around 1.3 billion dollars in its unauthorized dealings[2].

As far as the bankruptcy of Lehman Brothers (2008), one of the oldest and largest investment bank, is considered, it is the result of a "miscalculated exposure to mortgage-backed securities (MBS) and other collateral debt obligations (CDOs), an error which proved fatal after the collapse of the US housing market" (Global, 2023). Satyam scam (2009) is considered as India's biggest accounting fraud. It was a clear fraud that misled shareholders, stock exchange, and board of directors with accounts showing grossly inflated profits making it looking financially healthy in connivance with the auditors and chartered accountants (Correspondent, 2015). Tata finance case arouse as a result of series of fraudulent transactions leading to material misrepresentations in the financial statements of the company (Knapp, 2011). Sahara Pariwar case witnessed the battle between Sahara pariwar and capital market regulator SEBI over the company's fraud and causing a loss of more than Rs. 24,000 crore to thousands of investors[3].

V. CORPORATE GOVERNANCE IN INDIA

It was the galloping corporate frauds and scams that led to the constitution of corporate governance codes in India too. The foundations for the code in India was laid down

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based on the recommendations of various committees like Cadbury committee, Kumar mangalam committee, Green bury committee, Kings committee, Security exchange commission, Narayana Moorthy committee, Naresh Chandra committee and JJ Irani committee on corporate governance.

The framework on corporate governance in India included the following after incorporating international standards and procedures:

1. The Companies Act, 2013, which has provisions concerning Independent Directors, Board Constitution, General meetings, Board meetings, Board processes, Related Party Transactions, Audit Committees, etc.

2. SEBI (Securities and Exchange Board of India) Guidelines, which ensure the protection of investors and have mandated the companies to adhere to the best practices mentioned in the guidelines.

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

4. Standard Listing Agreement of Stock Exchanges, that applies to the companies whose shares are listed on various stock exchanges.

5. Secretarial Standards Issued by the ICSI (Institute of Company Secretaries of India) issues standards on 'Meetings of the board of Directors', General Meetings, etc. The companies Act 2013 empowers this autonomous body to provide standards which each and every company is required to adhere to so that they are not punished under the Companies Act itself (India, 2018).

VI. ORGANIZATIONAL AND OTHER DIMENSIONS

When we look at the various organizational dimension of corporate governance in India, remarkable inferences can be drawn, for instance, from banking sector, small and medium enterprises, public enterprises, financial sector enterprises, energy sector enterprises, etc.

Regarding the banking sector, studies reveal that, the size of the Board of Directors and shareholder pattern do have significant influence on the financial performance of the banks. More specifically, the Board size influence the Non-Performing Assets (NPA) of the public sector banks whereas executive directors lever the profitability of private sector banks. Shareholding pattern is found to be significant for both public and private sector banks, with more influencing private sector banks (Mishra & Rao, 2013). As far as small and medium enterprise in India is concerned, it has been found that they give good prominence to corporate governance practices (ASCI, 2015). Corporate governance practices play salient role in public and financial sector enterprises and its performance as well. People began to distinguish between those companies that follow corporate governance codes and those who do not follow. This has improved the level of adoption of corporate governance practices among the corporates.

In case of energy sector enterprises, studies reveal some crucial facts. One of such fact is that, the old companies in the sector are less adoptive towards corporate governance practices. Adding to it, the higher profit earning companies have less corporate governance compliance despite having strong audit committee and Board (Dube, et al., 2013).

Moreover, it is interesting to find E-governance as a new dimension in India along with the role of 'Gender diversity' in corporate governance and its impact on the corporate performance. E-governance can be extended to a next level of e-corporate governance as demanded by a democratic nation like India (Charan, 2011). As ICT enabled technology is advancing, e-corporate governance can be a more effective way to implement corporate governance and transparency in it. As far as gender diversity is addressed, studies point out that there is still a lot to go for corporates. A report reveals that "the distribution of women directors in various industrial sectors has been found to be quite skewed with 12 of the industrial sectors comprising a total of 24 companies had only two women directors on their boards" (Bansal, 2014). The report also shows that when compared to public companies, private companies have a positive graph towards gender diversity.

VII. CONCLUSION

The rise of corporate governance marked when the demarcation of owners and management began. The sprinting accounting and financial frauds across the nations led to the legalization of corporate governance as a mandatory clause. Analyzing the various dimensions including the organizational dimensions of corporate governance, it can be seen that the role of corporate governance has increased only. The need for strong corporate governance still continues.

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