CHAPER IV
BOARD OF DIRECTORS

4.1 Introduction
4.2 Rationale of the Board
4.3 Unitary Vs Two -Tier Board
4.4 Types of Board
4.5 Functions of A Board
4.6 Board Meeting
4.7 Annual General Meeting Vis – À - Vis Directors
4.8 Nature of a Board
4.9 Transparency
4.10 Independence of the Board
4.11 Attitude of the Secretaries Towards the Board
4.12 Conclusion
Thou shalt not ask questions.
Thou shalt not dissent seriously.
Thou shalt not rock the boat.
Thou shalt not blow whistles.
Thou shalt not demand liability insurance coverage.
Thou shalt not call for recorded votes.
Thou shalt not investigate issues.
Thou shalt not strive for perfect attendance.
Thou shalt not mind the shareholders.
Thou shalt not study the meeting agenda.¹

4.1 INTRODUCTION

The present chapter examines the rationale of the board, its function, composition, classification and nature. The present researcher also attempts to examine how the board meeting is being conducted and how the directors participate in the annual general meeting. The board is supposed to be an independent body. It is responsible to constitute the second-tier management of the company. This aspect is also being examined. In order to ascertain to what the secretaries feel about the independence of the board members, the researcher makes an attempt to measure the attitude of the secretaries towards the board members. An ideal board should be transparent in providing as much information as possible for the shareholders. The performance of the board with respect to this aspect is also being analysed in this chapter. The current scenario in Indian companies with reference to corporate management is to be portrayed. The present researcher has developed a model to measure the effectiveness of the board process, under the name of Board Room Practices Model. With the help of this model, the boards of the respondent companies are attempted to be categorised in to Best, Good and Poor Board.

4.2 RATIONALE OF THE BOARD

A corporation represents an amalgam of disperse social interests. The interests belong not only to the present living generations but also to the living generations yet to come. It has and it wields enormous economic and social prowess. Those in control of the corporation, therefore, hold enormous responsibility of multifarious dimensions social, economic, ethical, scientific and technological. The effectiveness of any company board is largely dependent on its structure.

Unlike the sole-proprietorship or partnership, where the ownership and management responsibilities go together, there is a divorce of ownership and management functions in the company form of business. The shareholders are the real owners of the company, but due to various reasons it is neither practicable nor desirable to have direct management of the company affairs by the shareholders themselves. The shareholders wield the ultimate power and control over the affairs of the company. However, their role is nominal and the effective powers of management are vested in their elected representatives. Thus the nature of company management is more like a parliamentary democracy.

The reasons for delegating the authority of the owners to the board are:

The number of shareholders (members) of most companies is so large that it is practically impossible for all of them to participate actively in the management the company.

The shareholders are usually scattered over a wide area both within and outside the country. It is, therefore, physically impossible for them to come together to determine policy or to run the day-to-day management of the company.
The shares are freely transferable, in the case of a public limited company. Hence, there will not be continuity in membership as and when shares are transferred.

The complexity and volume of business require skilled managers to manage such businesses. Shareholders who come from different walks of life, cannot be expected to possess such varied skills required for different occasions.

The shareholders of companies are basically, investors. The primary motive of the shareholders are not to take an active role in participation in the day-to-day management. Their primary aim is to get return in the form of dividend, appreciation in the value of the shares and bonus shares. Hence, many of them would not like to take part an active role in the business. They are satisfied with a decent return.

Thus for practical reasons the powers of the management have to be delegated to a small body of elected representatives. The elected representatives are known individually as directors and collectively as Board of Directors. Section 253 of the Companies Act, 1956 provides that no body corporate, association or firm can be appointed as director of a company. Only an individual can be appointed as director.2

"The board of directors are the brain and the only brain of the company, which is the body and the company can and does act only through them." "When the brain functions the corporation is said to function."3 "Successful firms, whether large or small, are one in which the Board, the shareholders and the employees have a common purpose because they each know that their long term wealth, health and happiness depend upon the long term stability, growth and prosperity of their company."4 The important duties of the directors are to

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comply with the law, to keep the chief executive carry out his responsibilities and to act as trustee for the shareholders. The effectiveness of a board can be enhanced or restricted by the limitations or strengths of its individual members of the board. A confident board is open about the extent to which it adds value and is willing to identify, discuss and tackle barriers to its own contribution. The activities of the board should be as far as possible transparent. The board should maintain a proper balance between short-term priorities and securing long term future of the enterprise. Short-term pressures should not be allowed to drive. The board should attempt to convert the problems into opportunities.

The elected representatives of the shareholders, Board of Directors, collectively constitute the executive organ. The executive organ, in turn, appoints a second tier of management personnel, to look after the day-to-day affairs of the management. The executive organ reviews the decisions of the second tier organ constituted by them, counsels it and make changes whenever their performance is not satisfactory. Different countries have different names for the organ that appoints and supervises the second tier of the management, board of directors, supervisory board, and conseil d'administration. Different countries provide for different membership. Members of management board cannot sit on the German supervisory board but are permitted to do so under American, British, and Japanese law. In France, the top-management function is conceived as delegated by the board of directors to one or several of its members so that board membership is almost obligatory for membership in top management. And there are other variants. Outside of countries of the German-type company law, where this is forbidden, it is not uncommon to find boards in which membership is restricted to full-time members of management. In Japan, for instance, the board is usually another name for the top-management committee. In Great Britain, there is a distinction between executive members.

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of the board, that is, top-management people, and non-executive members, that is, outsiders who hold no official position in the company. Nationality is a criterion for getting membership in to the board in some countries. In Indonesia, only citizens are allowed to accept directorship of Indonesian companies, except in foreign investment companies. Citizenship or nationality is not a bar to accept directorships in companies in India. The way in which the primary board manages the second tier management organ varies from company to company even within the same country.

4.3 UNITARY VS TWO-TIER BOARD

There are two types of board structure, across the world, viz., unitary board and two-tier board. The unitary form of board is common in U.K. and common wealth countries. The-two tier boards are in use in countries like Germany, Austria, Argentina etc. In erstwhile colonies ruled by European nations other than U.K., two-tier board is popular. The unitary structure is the most popular board structure in the Anglo-American model. Similarly, the two-tier structure is extensively adopted under the German model of corporate governance.

The Cadbury Committee, which was set up in U.K. in May, 1991 by the Financial Reporting Council, the London Stock Exchange and the accountancy profession, to address the financial aspects of corporate governance, fortunately or unfortunately, dealt with in detail about the board structure. The committee concentrated much on the board purpose and functioning. Therefore, now a question arises regarding the suitability or modification of the existing board structure. Whether the form of unitary board is well equipped to fulfil the role of the board in corporate governance? Whether two-tier structure will enhance

the efficiency of the board by removing the defects of the existing board structure?

Under the two-tier structure, the upper tier, known as supervisory board supervises and reviews the functioning of the lower tier, which is known as a management board. The management board looks after the day-to-day management. It frames the policies and strategies. Normally membership is restricted to any one of the board. The same individual cannot occupy the directorship in both the boards. Whereas under the unitary structure, only one board is in existence. The day-to-day affairs of the business is carried on either by an individual or committee under the supervision of the Board of Directors. Usually, the powers of the management are delegated to a single individual. The Companies Act, 1956 permits the delegation of power by the board either to a managing director or manager. The managing director or manager chooses his own team and runs the show. The directors of the board also can participate in the day-to-day business. Thus, an individual can be a member in the board as well as in the management team. Generally, dual representation is not forbidden under the unitary board structure unlike the two-tier board.

The two-tier structure, though theoretically attractive, has serious flaws. In practice, this structure keeps the supervisors at a distance from managers whose performance they are supposed to monitor. Hence, the structure can review the operations in an unbiased manner. However, in reality supervisory Boards do not meet frequently and act slowly. They are often not kept informed. Though they have the right to demand additional information and to make certain management decisions conditional on their approval, these rights are seldom used. The reason is that, the members for the supervisory board are usually recommended by the management board. Hence the accommodation of a member in the supervisory board is in the hands of the management board. Therefore, the review is a biased one as well as ineffective. Similarly, in the countries where the unitary board structure is followed, a great debate is going
on about the efficacy of the unitary board. Though such boards have the advantage of cohesion, they are not designed to deal effectively with conflicts of interest or with reviewing performance. The need for training has not been adequately addressed in such boards. It should be a requirement. However, the two-tier model also suffers from its own limitations. Even if one attempts to import the two-tier model as such, the model is not problem-free. The legal responsibilities of all directors should remain the same, otherwise the non-executive would become a form of second-class director which would not be in shareholders’ interest.\(^7\) Moreover, such new-structure may be different only in form rather than in substance. Whether in unitary board system or two-tier system, the top tiers, the supervisory board in Germany and the directors under the unitary board model tend to let effective control slip out of their hands. The second tier’s eager CEO, and the equally eager counter-part of German Vorstand, assume control by default of the first tier. Even when the first-tier retains the control, it too often gets into ineffective hands.

The primary difference between the Anglo-American model and the German model is that the latter provides for representation to the employees in the board whereas it is not mandatory in the former, apart from the cosmetic difference of single-tier and two-tier structure. The German corporate boards are practising the concept from the early days, i.e. as early as 19\(^{th}\) century. Even in such countries, the issue of labour representation in the board, is not a settled matter. Though a legislation was passed in 1976 empowering labour representation in the board, it has become a subject of litigation in the court of law. Then the West German highest court reiterated that the near-equal labour voice on supervisory boards of large companies does not infringe on the property rights of shareholders because they still have a slight voting edge i.e., Chairman’s casting vote. “While giving the unions a big victory, West

\(^7\) “The Committee on corporate governance. (The ‘Hampel Committee’) A response from PIRC Limited”, www.pirc.co.uk, 10th February 1997.
Germany's highest court also left the door open for further action if the supervisory boards don't function as hoped. If however, the existing legislation isn't adequate to safeguard effectively the independence of the boards, it will be up to the lawmakers to provide a remedy. Therefore adoption of the Germany model as such in a country, where they are following unitary structure, will create problem in switching over. When the labour representation is not yet settled in a country where it is prevalent for more than a century, it cannot be implemented in a country, where it is not possible to give labour representation at the board level even in the public sector enterprises. The irony is the constitution's directive principles insists upon labour representation.

Thus structure is not important. Even in a unitary board, non-executive directors may act effectively both as team mates of the executives and as well as their referees. The moot question is can we have enough numbers of 'good quality and genuinely independent' non-executive directors. Companies would be able to induct genuinely independent directors provided appointments are made not on the basis of 'old school tie network', the prevailing current practice in our country as well as our mentor, viz., U.K.

### 4.4 TYPES OF BOARD

The National Association of Corporate Directors (NACD) defines the purpose of the board as follows. "corporate governance ensures that long term strategic objectives and plans are established and that the proper management structure (organisation, systems and people)is in place to achieve those objectives, while at the same time making sure that the structure functions to maintain the corporation's integrity, reputation and responsibility to its various constituencies". The definition is purposely broad in scope because it must

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cover a great variety of boards, most of which change and adapt over time. To illustrate, this variety, the NACD groups all boards into four functional categories:

a. Minimum boards meet only to fulfil statutory requirements.

b. Cosmetic boards serve as rubber stamps to management prerogatives.

c. Oversight boards function primarily to review programs, policies, proposal reports, and performance of managers.

d. Decision-making boards are involved in setting corporate policy, determining management objectives, and authorising their implementation.10

Many Indian boards either come under this first or second category. The first generation companies mostly belong to this category. To fulfil the legal requirements, a board will be prevalent. The family members will be in the board, if the company is able to mobilise funds within their friends and relatives circle. If they are not able to mobilise the funds, then the promoter will go for a public issue. Under such circumstances, persons from outside the family will be accommodated in the board, to woo the public or impress the public with some widely known personalities. As a result, India’s only Field Marshal, General Maneckshaw adorned the board of some companies. Retired deputy governors of Reserve Bank of India were accommodated in some boards. The promoters are able to sell their companies among the investing public. Such boards mostly come under this category.

Many Boards have “cross directorships”. People are invited to sit on boards because of their names. In return of the managing director of Company A accepting the board membership of company B, the president of company B accepts board membership of company A. In this way, many Indian companies
belong to the second model. There may be a reciprocal understanding that will avoid unnecessary questioning in the board meeting and embarrassing situations. These busy people do not have a large enough stake in the company to justify their spending much time on it. Or, if they are doing business with the company, they are understandably reluctant to probe into its affairs, to ask inconvenient questions, or to appear critical. They go through the motions. And they are likely to sit on so many boards that they cannot really do their homework. In India, directorships of companies was looked upon as something like becoming a member of an old boys’ club. To call on the great and the good outside the charmed circle may be to invite trouble.

Boards constituted for the purpose of review of the performance or decision-making function is countable in Indian context. Professionally managed companies, normally belong to MNC group. Companies belonging to TATA house, and of late, some companies, which believe in professionalisation, constitute the board for these purposes.

From a slightly different perspective, following an evolutionary progression, corporate directorates can be classified in the following manner:

a. Constitutional boards
b. Consultive boards
c. Collegial boards
d. Communal boards

The above classification considers the locus of power and the increasing significance of directors in the corporate governance mechanism.

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4.4.1 Constitutional boards

Constitutional boards are akin to minimum boards. The major difference is that the constitutional board emphasises the legal mandate each corporation receives from its creator, i.e., the Companies Act. As previously mentioned, every company, from the minute to the largest company, gets its right to legal life from the sovereign, who technically has the power not only to create a corporation but also to dissolve it. In the act of creation, the state issues a corporate charter which generally includes a provision that the new entity have a board at least with two directors in the case of a private limited and three in the case of a public limited company. Thus the company's constitution prescribes the board. Unfortunately, while they fulfil the legal mandate, most constitutional boards do little else. The directors tend to be unobtrusive and let all authority gravitate to the CEO. This characteristic is most prominent in small, new, low technology, closely owned firms, particularly if the company is run by the first generation entrepreneur. In the case of first generation entrepreneurs, mostly the board is of this type only.

Constitutional boards also carry other hereditary traits, depending upon their inception from proprietary or syndical parentage. Proprietary, in this instance, refers to founder-owner-managers who run the enterprise as a monarch. They are ready to delegate the powers only when there is a dire necessity to officers, who then serve as officers or inside directors. Syndical refers to ownership and power concentrated in a group of financial entrepreneurs who do not attempt to run the firm actively. Instead, even while serving on the board, they give nearly unqualified control to strong CEO. Over the time, the syndicate members relinquish their boardroom seats to outside directors who, in earlier days, served passively as cosmetic boards.

Many of the boards of Indian companies belong to this category, especially if the company is promoted and run by the first generation
entrepreneur. Companies run by the second generation or third generation heirs normally do not fit in to this model. According to Mr. R.K. Talwar, former banker, “For what purpose are board meetings held? It is not a cynical view, but a portrayal of reality to say that the purpose is more to meet the legal requirements than with the objective of involving the directors in decision making and securing policy guidelines”. It is jocularly reported that the company secretary of a Bangalore based company informed the chairman as follows “The directors have informed that all of them would be attending the board meeting, since no important issues are to be discussed. They all would be very happy to join the picnic to Brindavan Gardens in Mysore”. Barring a few companies, the board is nothing more than a statutory fiction. It is far from being an instrument of collective thinking. Companies belonging to TATAs and Birlas will not come under this category.

4.4.2 Consultive Boards

Consultive boards are the products of evolutionary progression. With growth in scale and complexity of endeavor, the dominant CEO finds it more difficult to act as the unquestioned helmsman. He needs either technical assistance, buyer-seller contacts, or legal, financial, or political advice. The logical source of aid is the board. If the CEO adds lawyers, bankers, or other business people, he fabricates an outside board of directors. If he leans on his key executive and gives them titles as directors, it then becomes an inside board. In either case, over a period of time, the directors become better educated, better qualified, and as ownership tends to be more diffused, more independent. Also, as operations become more complex and global, and as it customers, suppliers, government, and the general public take a keener interest in the firm, the CEO must consult more seriously with his board. Currently, the great majority of American boards are consultive in function. Indian companies have not graduated to this level still. As observed earlier, many of the Indian companies
are still in their infancy. With the arrival of the new breed of investors, in the post liberalisation era, shareholders started questioning the companies for their performance. Financial institutions started reacting to the performance of the company, unlike in the earlier period. It is a period of transition. In the pre-LPG era, most of the companies belong to the constitutional boards. In the near future, more companies may come under consultive boards.

4.4.3 Collegial boards

Collegial boards are the next logical stage in the governance progression. Broadly diffused public ownership is an absolute prerequisite for collegial boards. There must also be string countervailing power coalitions within the board and the corporation. These power coalitions serve to minimise the prospects of one-man rule. Sometimes a benevolent despotic CEO will try to convey the image of collegiality, but real collegiality needs more of a permanent checks-and-balances, coalition structuring. Collegial meetings are characterised by discussion, debate and disagreement. Differences of opinion are resolved by a vote, a majority vote prevailing. Of special significance is the fact that disagreement with the majority or with the CEO does not mean dismissal from the board. Collegial boards meet more frequently than constitutional boards (usually quarterly) or consultive boards (from ten to twelve times a year). This characteristic, meeting as frequently as needed, means that all directors must be available at all times; otherwise power gravitates into the hands of those present. Moreover, if a director is to perform in meaningful collegial fashion, he or she must be a technically proficient professional manager.

Only a handful of large publicly owned corporations in U.S.A. have even the semblance of collegial boards. The era of the collegial board is still a distant dream in U.S.A. Therefore, one need not wonder about the status of Indian

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boards. Most of the boards of Indian companies come under the first category. As observed earlier, it is a transition period from first category to second category. Therefore, the era of collegial board is only a fiction in Indian context.

The most serious obstacles to widespread use of collegial boards in business are the slowness and indecisiveness of such group actions. Petty jealousies, preconceptions, and vested positions tend to slow down the collegial decision-making process. All the imperfections and inefficiencies associated with committee action are typified in collegial boards.

4.4.4 Communal Boards

Communal boards in one context, are public boards. Their membership closely parallels the composition of the political authority. The shift in the public enterprises board, whenever, there is a change of power, is a best example for the communal boards. The recent move of the Government to give an accommodation to small shareholders in the board is another example for the communal boards. Employees representation in the Supervisory Boards of German is yet another example of communal boards. The important consideration is that if boards of directors, constitutional, consultive, or collegial, lose their vigour and fail to satisfy society’s needs, them communal boards will become more likely prospects. Such representation is hard to see in Indian context, except in the public enterprises. The prime objection to any form of communal control in our governance mechanism is its super systematisation; all pertinent components are rigidly fixed within the infrastructure; all response are automatic, predictable, and compliant. Conformity and regimentation prevail. This is the domain of the bureaucrat. While there are many benefits which follow from bureaucratisation, the cost in terms of curtailed freedom, reduced motivation, and stifled initiative is high. The present legislative provisions are not in support of this model. Though the Companies Act is amended to give
berth to small shareholders, it remains to be seen, whether, the provisions are going to be implemented or not.

Table 4.1 summarises and contrasts the four basic board types (constitutional, consultive, collegial, and communal) on four norms: (1) the reason for the board, (2) its authority form, (3) who is the decision maker, and (4) the board’s decision-making role.

Table 4.1

<table>
<thead>
<tr>
<th>Types of the Board</th>
<th>Constitutional</th>
<th>Consultive</th>
<th>Collegial</th>
<th>Communal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reason for board</td>
<td>Legal</td>
<td>Economic</td>
<td>Socioeconomic</td>
<td>Political</td>
</tr>
<tr>
<td>Authority form</td>
<td>Autocratic</td>
<td>Oligarchic</td>
<td>Technocratic</td>
<td>Bureaucratic</td>
</tr>
<tr>
<td>Decision maker</td>
<td>Chief executive</td>
<td>CEO plus key executives</td>
<td>The board</td>
<td>Central planning agency</td>
</tr>
<tr>
<td>Board’s decision-making role</td>
<td>Acceptive</td>
<td>Advisory</td>
<td>Definitive</td>
<td>Adaptive</td>
</tr>
</tbody>
</table>

Source: Stanley C. Vance, Corporate Leadership – Boards, Directors and Strategy, McGraw-Hill Book Company

The particular board type, which will be used, will depend upon the prevailing milieu, that is, the composite of socio-political-economic forces, which shape a given society at a given time. The important consideration is that every milieu reflects the aspirations and accomplishments of its members. A society that recognises the need for enterprise, innovation, and equity will sanction, gestate, and perpetuate appropriate governance mechanisms.

To assess the nature of the boards of companies in Tamil Nadu, the present researcher has constructed a questionnaire. The question bears number 24 in the questionnaire.
Q.24. Decisions in the Board Meeting taken by:
(i) CEO
(ii) CEO + Key Executives
(iii) Entire Board

Table 4.2

<table>
<thead>
<tr>
<th>Decisions Taken By</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>CEO</td>
<td>37</td>
<td>47</td>
</tr>
<tr>
<td>CEO + Key Executives</td>
<td>29</td>
<td>37</td>
</tr>
<tr>
<td>Entire Board</td>
<td>12</td>
<td>16</td>
</tr>
</tbody>
</table>

Source: Primary Data

The survey results revealed that 47 per cent of the companies board can be classified into constitutional board type, where the decision is taken by the CEO himself. 29 per cent of the boards comes under the category of consultive boards as the CEO takes the decision in consultation with the key officers, and only 16 per cent of the boards can be grouped under the collegial model, on the basis of decision-making authority. As the companies taken for the survey belong to the private sector, the communal model was not considered and hence no question was set for testing whether the board belongs to the communal model or not.

Further to conform the nature of the board the following question was framed constructed and included in the questionnaire.

“Q.13. Purpose for the conduct of the Board Meeting:
(i) To satisfy the legal requirements
(ii) To evaluate the performance of the company
(iii) To frame the policy for the future”
Table 4.3
Purpose of the Board meeting

<table>
<thead>
<tr>
<th>Purpose of the meeting</th>
<th>Number of companies</th>
<th>Percentage of companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>To satisfy the legal requirements</td>
<td>61</td>
<td>78</td>
</tr>
<tr>
<td>To evaluate the performance of the company</td>
<td>78</td>
<td>100</td>
</tr>
<tr>
<td>To frame the policy for the future</td>
<td>33</td>
<td>43</td>
</tr>
</tbody>
</table>

Source: Primary Data

As per the response given by the secretaries of the companies who had responded, all the companies conducted board meeting for the purpose of evaluating the performance of the company. In addition to the review function, 78 per cent of the companies had agreed that they were conducting the board meeting for satisfying the legal requirement. Only 43 per cent of the companies were using the board meeting for framing the future policy. Again, the responses revealed that Indian boards fell in between the constitutional and consultive boards.

By virtue of section 291, Board of Directors is the executive organ of the company. In turn, the Board of Directors can appoint employ one or more than one of the following categories of managerial personnel, viz., a. managing director and b. manager. According to the Companies Act, the management vests directly in the Board of Directors and no chief executive need be employed. Though legally, a board can run the show directly without creating a second tier management team, no company in India is functioning without the CEO.

To ascertain the position, viz., who manages the company – whether the CEO or manager or the board - in India, the present researcher constructed a question. The relevant question bears number 74.
Source: Questionnaire

The survey results revealed that all the companies have been managed by managing directors. In some companies the position of managing director is merged with that of Chairman. In some other companies the companies are managed by two managing directors. But no company is functioning either with a Manager or by the board directly without the presence of a managing director. To classify the board as constitutional, one needs to have a shareholding pattern. If the size of the holding of the promoter is known, one can clearly conclude whether the board is constitutional board or not.

4.5 FUNCTIONS OF A BOARD

By virtue of section 291 of the Companies Act, 1956 Board of Directors is the executive organ of a company. The members of the board, individually have in fact no function or duty whatsoever. The board is essentially a group and collective activity. Detailed management is not the responsibility of the board and indeed a board which attempts to perform detailed functions, not only runs the risk of overstepping its functions but also runs the risk of performing a very inadequate task. Because it does not have the depth, knowledge of internal functions and the executive powers to carry on the functions of day-to-day detailed management. There are actually three different tasks for which a company needs a functioning board.\(^\text{13}\)

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The enterprise, first does need a review organ. It needs a group of experienced people, people of integrity and stature, people of proven performance capacity and proven willingness to work, who counsel, advise, and deliberate with top management. The score of Indian board with reference to this factor is satisfactory. All the companies responded to the relevant question, question number 13, indicating that one of the purpose for the conduct of the board meeting is to review the performance of the management. The analysis of the relevant question was presented earlier in Table 4.3 of this chapter.

Yet another question was asked to evaluate the functions of the board. The relevant question bears the number 14 in the questionnaire. The respondent was asked to assign suitable weightage to a number of businesses that were normally transacted. Among the transactions, the transaction which received the maximum attention was discussion of financial results and discussion on day to day operation. Almost all the companies surveyed had responded that one of the businesses that was transacted by the board was discussion of financial results, a review function. 66.67 per cent of the companies resorted that they also carried on the discussion about day to day operation. Therefore, one can conclude that the companies listed in Tamil Nadu are on the right track vis-à-vis this function, viz. review function.

The second function to be performed by a board is with reference to the CEO. The board is going to manage the day-to-day affairs only through the CEO. Therefore, the success or failure of the company depends upon the single individual, because the entire administration is going to be looked after by the CEO. Hence, the board has to be more careful in his appointment. It has also to monitor and review his performance. It has to duly reward him for his performance. Similarly, remedial action has to be taken for the mistakes committed by him. If necessary, the CEO should be fired. A functioning board is needed to remove a top management that fails to perform. A board capable of removing incompetent or non performing top management has, of course, real
powers. And no society can tolerate top-management incompetence in its large
businesses. If a company do not have such an effective board, it is a loss to the
society.

In the U.S.A., one can see such effective boards. When the board acts
and installs new CEO and, if necessary, reshuffles the second-tier management,
the management literature calls it as board activism. A number of incidents can
be cited to illustrate such board activism. The General Motors boardroom coup
of 1992 was followed over the next few months by more corporate boards rising
up to sack under performing CEOs. IBM, American Express, Kodak,
Westinghouse, and over the rest of the 1990’s other major firms, such as K-Mart.
Apple computer’s board seemed to change its CEOs more often than it changed
operating systems. Apple also gave the ultimate proof that the board today
matters in the health of a company. After it’s latest CEO firing last July, founder
Steven Jobs came to the board and pointed out that, while CEOs had come and
gone, results had continued to slip, and the real constant problem had been the
Apple board. He convinced the board to restructure itself, adding more tech-
savvy industry leaders. It proves that the board matters, when it can accept itself
as part of the problem.

A recent example in the American corporate sector is the case of Lucent
Technologies, telecommunications equipment maker. “Struggling
telecommunications equipment maker Lucent Technologies” ousted chairman
and chief executive Rich McGinn, replacing him with former chairman Henry
Schacht, and slashed its sales and profit outlook for the first quarter of 2001.
Some analysts called Lucant’s decisions to fire Mr. McGinn Lucent’s long
overdue. Lucent cut its growth forecasts four times this year, introduced new
products later than its competitors, and failed to keep up with customer demand
for optical networking products. “They should have got rid of McGinn after
Q1(of 2000), but the board didn’t know what to do. The board was all
handpicked by McGinn. With a new person coming in, I think they will all be
gone too. It will be a whole new board," said Frank Dzubeck, president of consulting firm Communications Network Architects. When it became clear that Lucent’s problems would linger into the first quarter of 2001, the board was forced to cut Mr. McGinn to show investors that the company was committed to turning itself around, analysts said. “In a meeting this weekend, the board reviewed Lucent’s recent performance and outlook for the current quarter and determined that an immediate change in leadership was necessary,” the company said in a statement.14

Such experiences are rare in Indian context. In most of the companies in India, the promoters are the major shareholders, holding around 50 fifty per cent of shares. The constitution of board process is slightly different, from the way it is used to be constituted in developed countries. Here, the promoter chooses his board member and constitutes the board. The board members are at the mercy of the incumbent management, viz., promoters or his appointees. Therefore, the process works otherwise. Usually, the board chooses the CEO and monitors the performance of the CEO. However, in India the promoter chooses his board in order to satisfy the legal provisions. Unless and otherwise the promoter is dissatisfied, the CEO and other board members are free to continue, despite their poor performance. Here also review takes place and dismissal also happens once in a while. However, the firing and hiring is not the privileged function of board. It may be the decision of a single individual.

The same situation prevails with respect to the companies which are run by the second and third generation entrepreneurs. Even companies belonging to TATA group can be cited as an example, where the whims and fancies of the Chairman of Tata and Sons prevail over the members of the board. The personal reason may be the only factor in the removal of some of the directors in TATA group companies. It is purely a personal decision of the group chairman, regarding the hiring and firing of both the CEOs and the board members.

In Indian context, where shareholders’ activism is at nascent stage, only institutional shareholders can exercise certain amount of control through their representatives in the board. Unfortunately, at times even such institutional shareholders’ representatives in the board are thrown away from the board through the annual general meeting. Once the nominee director of Shaw Wallace was sent out of the Board by passing a resolution in the annual general meeting. If that is the prevailing situation in India, then how one can expect, the board to be active in evaluating and monitoring the performances of the board. The Voltas case cited above and the regular under performing companies belonging to Tata group which are cited below, clearly portray the prevailing role of boards in hiring and firing CEO as well reshuffling the second-tier management. The reason for the reversal of the roles can be attributed to the attitude of shareholders towards performance in the earlier days – before the advent of globalisation – and the thumping majority of the promoters after 1994-95, where the promoters are allowed to increase the stake in the concern at a throw away price.

To ascertain the promoters’ holding and voting strength in the companies surveyed, the present researcher has included a question in the questionnaire. The relevant question bears the number 4 in the questionnaire. The responses to that question have been presented in Table 4.4.

<table>
<thead>
<tr>
<th>Shareholders</th>
<th>Percentage of Shareholding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Promoters</td>
<td>53</td>
</tr>
<tr>
<td>Financial Institutions</td>
<td>7.9</td>
</tr>
<tr>
<td>Individual Shareholders</td>
<td>39.1</td>
</tr>
</tbody>
</table>

Source: Primary Data

The results clearly show that the promoters enjoy a majority with 53 per cent. Therefore, the promoter can get easily passed any ordinary resolution without any problem. In some cases, financial institutions hold around 20 to 25
per cent. However, nobody except the promoter has the capacity to appoint directors, though the Companies Act, 1956 provides for proportional representation under section 265. Under this system, even the minority shareholders can have representation in proportion to their strength. However, the Companies Act gives an option to companies to provide for proportional representation for the appointment of directors. It is not a mandatory requirement. The option may be given through the Articles of association. If the Articles permit, two-thirds of the total directors may be elected according to the principle of proportional representation, either by single transferable vote or some system of cumulative voting. The present researcher has gone through the Articles of Association of all the companies taken for the present study. No company has provided for the proportional representation. Had it been made compulsory at least for one-half of the strength of the board, some of the present evils would have been checked.

The strong grip of the promoter in the board affects the review mechanism. It is loaded in favour of the promoters, due to the method of electing the directors. In reality, a review may be conducted, recorded in the minute book and ultimately the poor performances are justified. There is no exception to this rule in India. Crisis and severe crisis alone may precipitate a situation where the controlling authority is forced to effect some change. Another reason for this type of behaviour is that the environment is so congenial to even under performers. Being a sellers market, even a Tom, Tick and Harry can earn profits. Absence of competition enabled even the inefficient units to thrive on the strength of the protection provided by the Government. Hence even a review, if conducted, may not expose the culprit, because of the environment. Another reason for this indifferent attitude of the promoters towards the review mechanism is the attitude of shareholders. shareholders’ activism is a new term in the Indian corporate sector. Therefore there is no compulsion to change the under performer, if at all the CEO happens to be a
person other than the promoter or his relative. If the CEO happens to be a relative or a friend of the promoter, then that qualification is sufficient to justify the performance. Question number 64 of the questionnaire solicits information to find out the proportion of the CEOs who are relatives to the promoters. The responses of that question have been tabulated in table number 4.29. The responses indicate that 55 per cent of the CEOs are related to promoter or his group. Naturally, attempts will be made to protect the relatives of the promoter, by diverting the funds from some other public companies where the promoter is having the control. Apart from the group companies, the political support enabled the promoters to avail cheap funds from the public financial institutions. Once in a while, again with the blessings of the politicians some portions of the earlier loans may be waived. A critical point will be reached even such public financial institutions may not be in a position to rescue by pumping additional funds as the unit is beyond the critical stage. The public financial institutions refuse to accommodate such bleeding concerns. Even now the show is not over. Still chances are there for the inefficient promoters to plunder the wealth of the nation because of the existing legal frame work. Then comes the BIFR, to rescue the dying patient. The sick doctor, BIFR, will prolong the life of the patient, who is in coma. Thus, the review mechanism is by-passed in the Indian corporate sector to the advantage of the promoters. The above mentioned tactics is not the exception. It is the general rule.

The following report in a leading financial daily, prepared by its research wing, reveals that the TATA group have failed shareholders once again, indicating that such failure is not an occasional feature but a recurring and regular phenomena. “The Tatas have failed their shareholders once again. Despite a reasonably high growth in sales turnover and a sharp fall in the rate of decline in net profit in 1999-2000, the shareholders’ value of the Tata group of companies has dropped further. The shareholder’s value or the return on net worth (RONW), measured as net profits as a percentage of net worth of 20 large
group companies, has declined from 9.24 per cent in 1998-99 to 8.42 per cent last year. Incidentally, it was 11.9 per cent two years ago. The aggregate sales turnover of the sample companies has grown by 14 per cent during the period while the aggregate net profit declined by a little over 2 per cent compared to a fall of more than 21 per cent in 1998-99 over the previous year. This is disturbing. For, shareholder value does not merely indicate the material return that the shareholder receives, but it indicates the efficiency of capital and is used widely as an indicator of competitiveness. Of course, deceleration in RONW value alone is not enough to infer that the group’s competitive power has declined, but the fall surely has effected the investors’ morale. The group has lost comprehensively both in terms of market capitalisation and in trading volume in the current year. Eleven of the 20 sample companies have witnessed a fall in RONW while two, ACC and Tata Telecom, have negative values as both of them incurred a loss last year. Tisco, the flagship company of the group, has improved shareholders’ value – courtesy profit on sale of net assets of cement division. But Telco was not as lucky. Despite the profit on the sale of machine tools, heavy axles and heavy transmission business (Rs.134.34 crore), its net profit declined by over 27 per cent last year bringing down the RONW from 3.23 per cent in 1998-99 to 2.40 per cent last year. Of course, it came as no surprise. “As expected in the case of a major product introduction in a new business area, the company’s operating profitability was negatively impacted by the ramp-up phase of the Tata Indica car activity”, Ratan Tata has said. Maybe. But then how can one explain the declaration in the shareholders’ value of Tata Chemicals, Rallis, Indian Hotels or Voltas – none of which ventured into new areas in any major way in recent years?”

There is another alternative in the market driven model of corporate governance, to check such poor performance. The take-over attempt by a

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financial raider or predator will take care of such companies. Take-over attempts are the mechanism which is believed to be an effective check, in developed countries against poor performance. The poor performance, will send the market price of the shares of the particular company down. As shares become cheaper, other groups may be tempted to acquire the control of the company by buying the shares which may be available at the rock bottom prices. Having acquired sizeable volume of shares, the raider can get the control of the company. Management experts and economists have been telling us for a long time that the top management of large publicly held companies have become immune to stockholder control and that only coronary thrombosis or bankruptcy can dislodge a top management once it has established itself. Top management – most of them seemingly all-powerful, seemingly deeply entrenched, seemingly in complete control – have been toppled by stockholder revolts organised by the financial raiders and their “take-over bids”. The raiders did not aim at companies in trouble. They aimed at the companies that did not live up to their potential, companies the top management of which did not perform adequately. Unless top management builds into the company’s structure an effective organ for its removal in case of non-performance, the raider and his takeover bid will become an ever-present threat. A jackal is better than no scavenger.

Again, this mechanism is also prevented to function as had functioned in the other parts of the world. The reason being the protection given by the Government even to inefficient promoters. The patronage extended by the politicians created a congenial atmosphere for such under performer. Indian corporate world, for the first time, started experiencing this model, in early eighties. When Escorts and DCM were under the threat of take-over by Swaraj Paul, an NRI, overwhelming public sympathy was with Nanda and Shriram family. Small investors supported the incumbent management, though the companies were not performing well. People asked “Nanda has started Escorts
in a shed. How somebody can come and take-over his company. It did not
dawn upon the Indian psyche that Escorts is not the Nanda’s company. The
promoters were only the agents doing the business on behalf of the absentee
shareholders. This attitude also permitted the incumbent management to ignore
shareholders. Thus, the environment is conducive to the incumbent
management. Individual shareholders ignored the performance and they had
taken it for granted any performance. They never felt that their money is not
utilised properly. The more powerful institutional shareholders are also helpless
because of the political patronage available to the inefficient promoters. The
market mechanism also failed because of the attitude of the Government.

However, the attitude of the investors started changing with the dawn of
liberalisation. New breed of investors entered the market, who demand
performance. However, the SEBI enabled the incumbent management to
increase their shareholding to prevent any take-over threat at a throw away price
during 1993 and 1994. Most of the companies’ management increased their
stake at the cost of the outside shareholders. Those management who failed to
increase their stake during that period, were now subject to the take-over threat.
They alone have to respect the rule of the market. Therefore, those companies
whose management failed to increase their stake to more than 50 per cent, will
be checked by the predators.

An effective board, therefore, demands top-management performance and
removes top executives who do not perform adequately. This is the duty of the
board. An effective board asks inconvenient questions. An effective board
insists on being informed before the event – this is its legal responsibility. An
effective board will not unquestioningly accept the recommendations of top
management but will want to know why. It will not rubber-stamp the personnel
decisions of top management but will want to know, indeed to get personally

acquainted with, alternative candidates for senior appointments. An effective board, in other words, insists on being effective.

Another sub-function related to the second function quoted above is the succession planning. Though the current CEO may perform well, the board should groom a proper heir to the throne. Proper training is required, before one assumes the charge. Even if the legal heir of the promoter assumes the charge after the CEO, they should be properly trained before entrusting the Herculean task of managing the affairs of the business. Therefore, one may conclude that a board has performed well with reference to the second function, viz., selection of CEO, only if the succession planning is conducted. Hence the researcher has inserted two questions in the questionnaire to judge whether the board has performed the succession planning. The same question is asked one for the period prior to 1997 and after 1997. The reason for the selection of the period '1997' is that only after 1997 the term corporate governance has become a hot topic in Indian context. Therefore there is a chance for some companies to assume the succession planning at least after 1997. Had the company conducted the function prior to the period 1997, it is an outstanding company. We can appreciate that company in terms of good board practice. The relevant questions are:

"Q.71 Had the board involved in the succession planning exercise in the period prior to 1997?
Q.72 Had the board involved in the succession planning exercise in the period after 1997?"

The response for both the questions are negative, which have clearly communicated that no company was bothered about this function either prior to or after 1997. It seems that the all the CEOs are certain that they need not hand over the job to some one else. Perhaps the adage that nothing is permanent except change may not be applicable to Indian corporate set up. The CEOs as well as boards are always constant. Either death or some extraordinary circumstances may compel to shuffle the board.

Finally, the enterprise needs a “public and community relations” organ. It needs easy and direct access to its various constituents. It needs to hear from
them and be able to talk to them. The need is readily apparent for the big company, of course. But it may be even greater for the small or fair-sized company which is a major employer in a small or medium-sized community.\(^\text{17}\)

The central fact is that the modern enterprise has a multiplicity of constituencies. The shareholders are one. But they are no longer the one, as traditional legal theory has it. Instead of being “owners” they have become “investors”. The employees are clearly also such a constituency, but they are not, as the German trade unions (or the “industrial community” laws in various Latin-American countries) assert, the constituency. There are also the communities where a major company has its plants. There are consumers, suppliers, and distributors. All of them need to know what goes on in a major business, what its problems, its policies, and its plans are. The business needs to be understood by them. Top management needs to be known by them, respected by them, accepted by them. Top management needs even more, perhaps, to understand what these constituencies want, understand, misunderstand, see, question.

As pointed out earlier in Second Chapter of the present research report, the divergent practices of corporate governance are started converging. “The Shareholders Model of Corporate Governance” now started giving importance to other stakeholders. Similarly, the countries which are adopting Stakeholders Model like Germany and Japan are now concentrating on improving shareholders’ wealth. Therefore, at the world level, different practices are now converging. The third function arises as a result of giving importance to various stakeholders. As a result, the board is responsible to other stakeholders. However, in India where the shareholders’ model is followed, the incumbent management has not discharged its responsibility even towards their shareholders. Under such circumstances, it will become ridiculous, to expect the

management to discharge their responsibility towards other stakeholders. Hence the present researcher, does not attempt to measure, whether the board has discharged the duties with reference to the community.

In the words of Peter Drucker, "In reality, the Board as conceived by the law-makers is at best a tired fiction. It is perhaps not too much to say that it has become a shadow king." To quote Drucker again, "It is an organ of review or appraisal. Only in crisis, it becomes an organ of action."\(^\text{\#18}\) The problem of CEO domination is a universal phenomenon.

The situation prevailing in India is still more different. Right from the beginning, Indian companies have been managed through the Managing Agency System. As a result, from the day one, the Indian companies' boards are sidelined by the managing agency system. Even after the abolition of the managing agency system the promoters of the companies have stepped in to the shoes of the managing agency system and managing the show. In the absence of shareholders' activism, the promoters are continuing the practice, without any check. The boards have become a rubber stamp board. The CEOs tell what it suits them to tell the Board. The Boards become bored stiff with volumes of non-essential information. The non-executive directors have seldom an opportunity or the wherewithal to find out whether what they get is the truth or only a varnished version. In this context, there have been suggestions that non-executive directors should be equipped to ask and obtain information from within the company. But, it is also argued that this might detract from the line of command of the Chief Executive. Logic demands that non-executive directors should not merely mark attendance at the Board form frills and decorations to annual reports. An important set of questions concerns how the non-executive directors and the chairman if non-executive are selected. There is a story of how a promoter waited till most of his existing Board members died or

left and then packed his board with the kind of people who would give him unstinted support. Such people used to boast about it and claimed that their Board was more or less a black board. Barring a few companies, the board is nothing more than a statutory imposition and in any case is far from being an instrument of collective thinking. To ascertain the functions performed by the board and to get an ideal about the priority given among such businesses by the board, a list of possible businesses that can be transacted by a board is presented to the respondents. They were asked to assign suitable weight to the various businesses depending upon the importance given to such business in the board meeting. The relevant question bears number 14.

"14. Nature of the Business Transacted by the Board (Give weightage in Percentage)
(a) Discussion of financial results
(b) Strategy Planning
(c) Discussion about day to day operation
(d) Managerial succession
(e) Government relations
(f) Shareholders' relations
(g) Labour relations
(h) Any other (Please specify)"

The results of the responses were presented in table 4.5

<table>
<thead>
<tr>
<th>Nature of Business</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
<th>Weighted Average (Percentage) Score Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discussion of financial results</td>
<td>78</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Strategy Planning</td>
<td>60</td>
<td>78</td>
<td>78</td>
</tr>
<tr>
<td>Discussion about day to day operation</td>
<td>52</td>
<td>66.67</td>
<td>67</td>
</tr>
<tr>
<td>Managerial succession</td>
<td>27</td>
<td>35</td>
<td>35</td>
</tr>
<tr>
<td>Government relations</td>
<td>23</td>
<td>29.48</td>
<td>29</td>
</tr>
<tr>
<td>Shareholders' relations</td>
<td>17</td>
<td>21.79</td>
<td>21</td>
</tr>
<tr>
<td>Labour relations</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Any other (Please specify)</td>
<td>18</td>
<td>23.08</td>
<td>23</td>
</tr>
</tbody>
</table>

Source: Primary Data

All the companies surveyed agreed that ‘Discussion of financial results’ was a regular business as compared to labour relations, which was considered not at all by the board. Next to ‘Discussion of financial results’, comes ‘Strategy Planning’ which was considered as regular business of the board meeting. Though 52 companies have agreed that ‘Discussion about day to day operation’
is a regular business in the board meeting, the weightage given by the companies is 67 per cent compared to 78 per cent to Strategy Planning, where 60 companies treated it as a regular business. The trinity function calls for succession planning also by the board. However, only 27 companies have treated it as a regular business.

Another question on the similar line is included in the questionnaire to know to what extent the directors are interested in the above said businesses. They are also asked to rank the business in the order in which the directors show interest. The question is included as question number 15 in the questionnaire. The relevant question is:

"Q.15. Of the above Business, in which business the directors are most interested? (Please rank as 1,2,3,......)

a. b. c. d. e. f. g. h."

<table>
<thead>
<tr>
<th>Nature of Business</th>
<th>Scoring</th>
<th>No. of Companies</th>
<th>Overall Score</th>
<th>Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discussion of financial results</td>
<td>598</td>
<td>78</td>
<td>16.61</td>
<td>1</td>
</tr>
<tr>
<td>Strategy Planning</td>
<td>546</td>
<td>78</td>
<td>15.16</td>
<td>2</td>
</tr>
<tr>
<td>Discussion about day to day operation</td>
<td>303.33</td>
<td>58</td>
<td>8.43</td>
<td>3</td>
</tr>
<tr>
<td>Managerial succession</td>
<td>182</td>
<td>45</td>
<td>5.06</td>
<td>4</td>
</tr>
<tr>
<td>Government realtions</td>
<td>86.66</td>
<td>27</td>
<td>2.41</td>
<td>6</td>
</tr>
<tr>
<td>Shareholders’ relations</td>
<td>78</td>
<td>32</td>
<td>2.17</td>
<td>7</td>
</tr>
<tr>
<td>Labour relations</td>
<td>78</td>
<td>28</td>
<td>2.17</td>
<td>7</td>
</tr>
<tr>
<td>Any other (Please specify)</td>
<td>104</td>
<td>25</td>
<td>2.89</td>
<td>5</td>
</tr>
</tbody>
</table>

Source: Primary Data

The above responses clearly reveal that the business ‘Discussion of financial results’ draws the attention of the most of the directors. Next comes ‘strategy planning’. Though the general response to the labour relation is nil to question number 14, at the level of the directors’ perception, it draws the attention of the directors in 28 companies. To ascertain whether the board is
seriously conducting the review function, yet another item is included in the questionnaire.

"Q.28. Is the day-to-day performance of the company critically evaluated in the Board Meeting?
Yes  No"

Table 4.7
Performance Evaluation by the Board

<table>
<thead>
<tr>
<th>Practice of Evaluation</th>
<th>Number of companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>56</td>
<td>72</td>
</tr>
<tr>
<td>No</td>
<td>22</td>
<td>28</td>
</tr>
</tbody>
</table>

Source: Primary Data

The results indicate that 72 per cent of the boards are carrying out the critical function of reviewing the day-to-day performance of the company. Hence, the boards of Tamil Nadu companies are performing the first function as enunciated by Drucker.

Therefore in terms of the trinity function, viz., review function is the most prominent function in India. The CEO hiring and firing is not given so much importance, as perceived by their counterparts in developed countries like U.S.A. Similarly, the public relation function as perceived by Peter Drucker is not seriously considered in India.

The board is an executive organ. One of its functions is to review the performance of the management. The review function does not end with the review with the performance of the management headed by the executive supposed to be installed by the board. A normal board will review its performance also. Therefore out of anxiety and interest, the researcher made an attempt to find out whether such review function is attempted by the board. For that purpose, question number 43 is included in the questionnaire. The relevant question is presented below.
"Q.43 Any Review of the Board's performance conducted so far?"

The response to the above question is tabulated in Table 4.8.

Table 4.8

<table>
<thead>
<tr>
<th>Review of Performance</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>8</td>
<td>10.25</td>
</tr>
<tr>
<td>No</td>
<td>70</td>
<td>89.75</td>
</tr>
</tbody>
</table>

Source: Primary Data

It is unfortunate that nearly 90 per cent of the companies have accepted that no such exercise is ever conducted. Only some 10 per cent of the companies are involved in this soul-searching exercise. To probe the matter further, one more sub-question is included for the above question. This question is to find out the criteria adopted by the boards to evaluate the performance. Though 10 per cent of the companies have agreed that they are reviewing the performance of the board, no company has come forward to reveal what criteria they are adopting to judge the performance of the board. Therefore we have to contend ourselves that, the companies listed in Tamil Nadu are reviewing the board’s performance. The relevant question is included as question number 43a in the questionnaire.

"Q.43a. If yes, what are the objectives set for reviewing the performance"

The researcher attempted to solicit the information for the same issue once again, from a different angle. The information provided by the secretaries confirmed the responses they have provided earlier. The question is presented below, which is question number 44 in the questionnaire.

"Q.44. Is there any practice of setting of the objectives for the Board?"

The response to the above question is presented in Table 4.9.


Table 4.9

<table>
<thead>
<tr>
<th>Objectives Set</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>8</td>
<td>10.25</td>
</tr>
<tr>
<td>No</td>
<td>70</td>
<td>89.75</td>
</tr>
</tbody>
</table>

Source: Primary Data

10 per cent of the companies have stated that they are setting objectives for evaluating the performance of the board. Remaining 90 per cent of the companies have categorically stated that they are not setting any objectives for evaluating the board performance. Really, it is a sorry state of affair, that the top most executive organ of the company has not been subject to any performance review.

One more question related to the above question is included as question 44a. The relevant question is reproduced below:

"44a. If yes, is there any mechanism for the assessment of the board room performance?"

75 per cent of the companies who have positively responded for the question number 44, have stated that they have the mechanism. All the companies which have positively responded for question number 44, expressed that profit maximisation is one of the criteria. The second objective which is more popular with the companies is maintaining the market leadership.

To assess the functioning of the board, one question was included and the relevant question bears the number 73. The relevant question is given below:

"73. Had the company paid any penalty for the improper maintenance of statutory and non-statutory books?"

All the companies replied that they had not paid any fine. Great men think alike.
4.6 BOARD MEETING

The individual directors do not have any authority, in their individual capacity. It is an executive body. It can exercise the authority only collectively. Therefore the decisions of the board are taken only in the board meeting. Therefore the board meeting is the vehicle through which the functions of the board are carried out. The importance given to the board meeting by the company also reflects the importance given by the management to the board. It also reflects the efficiency of the organ viz., board. According to section 285 of the Companies Act 1956, a board meeting must be held at least once in every three calendar months, and at least four such meetings must be held in every year. It has been clarified by the Department of Company Affairs that, so long as four Board meetings are held in a calendar year, one in each quarter, the interval between two meetings of the Board may be more than three months. For instance, if a meeting of the Board is held on January 15, the next meeting may be held on 15th June, the third meeting on 15th July and the fourth on 20th December. That is, the interval between the meetings may be six months, one month or five months, as the case may be, but one meeting of the Board must be held in each quarter. The interval between two successive board meeting is not to be considered. An interesting observation with reference to the board meeting by Mr. R.K. Talwar, former banker: “For what purpose are board meetings held? It is not a cynical view, but a portrayal of reality to say that the purpose is more to meet the legal requirements than with the objective of involving the directors in decision making and securing policy guidelines”.19

The performance of the board can be evaluated with the help of a number of attributes of the board meeting. The following paragraphs are devoted to evaluate the vehicle of board meeting process:
Section 286 of the Companies Act, 1956 provides that notice of every meeting of the Board of Directors of a company must be given in writing to every director for the time being in India, and at the usual address in India. However, the Act does not prescribe any form of notice or the mode of service of notice of board meetings. Question number 8 is included in the questionnaire to evaluate the board effectiveness. The response to the above question is tabulated in table number 4.10.

Table 4.10
Notice for Board Meeting

<table>
<thead>
<tr>
<th>Notice (In days)</th>
<th>No. of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Upto 7 days</td>
<td>19</td>
<td>24</td>
</tr>
<tr>
<td>More than 7 days and upto 14 days</td>
<td>24</td>
<td>31</td>
</tr>
<tr>
<td>More than 14 days and upto 21 days</td>
<td>35</td>
<td>45</td>
</tr>
</tbody>
</table>

Source: Primary Data

It is really heartening to note that in 45 per cent of the companies more than 14 days notice has been given for the board meeting. It is a factor to be appreciated because even for the shareholders only 21 days notice is to be given by the company for the annual general meeting. Only in 24 per cent of the companies notice of less than seven days are given. From this angle one can infer, that the board meeting will be effective as sufficient notice has been given for the members.

4.6.2 Agenda

Agenda for any meeting is a must, if the meeting is to be purposeful and effective. There is no statutory compulsion to send agenda along with the notice of the meeting. However, a meeting is convened to transact businesses.

If the members of the board are not informed about the purpose for which they are going to assemble, the members cannot effectively contribute to the purpose for which they are assembling together. Such meetings are farce and of cosmetic nature only. Such boards can be grouped under rubber stamp board. Therefore, one can decide, whether the board is effective or not on the basis of this factor also, i.e., sending the agenda of the meeting ahead of the meeting. Hence, the present researcher has constructed a question to ascertain whether the company is sending the agenda along with the notice of the board meeting. The question bears number 9 in the questionnaire.

"Q.9 Is Agenda sent along with notice of the board meeting:
(i) Most of the times (ii) Less Frequently (iii) Rarely"

### Table 4.11

<table>
<thead>
<tr>
<th>Nature</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Most of the times</td>
<td>70</td>
<td>89.7%</td>
</tr>
<tr>
<td>Less Frequently</td>
<td>8</td>
<td>10.3%</td>
</tr>
<tr>
<td>Rarely</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>

Source: Primary Data

The responses to the question number 9 have been tabulated under Table 4.11. It is encouraging to note that 89.7 per cent of the companies sent the agenda along with the notice of the meeting. All the companies have the practice of sending the agenda. Hence, one can conclude that the board mechanism is fine and working well. It will be effective and contribute to the effectiveness of the board meeting.

#### 4.6.3 Venue

Yet from another angle, one can judge, what importance, the company management gives to the process of board meeting. If it is a ritual, no separate venue may be available. It is the top most organ of the management. It should
have a separate venue. If there is no separate venue in the company for the conduct of the board meeting, it speaks how well the management considers about the board. Can the CEO function without having a separate venue for his office? Hence, to judge the attitude of the management towards the board, question number 42 is framed, to solicit the information. The responses to the question has been presented in table number 4.12.

"Q.42. Which is the normal venue of the Board Meeting? If the venue is the Company's Registered Office is a separate Hall available exclusively for the Board Meeting? Yes No"

<table>
<thead>
<tr>
<th>Venue of the Meeting</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>61</td>
<td>78</td>
</tr>
<tr>
<td>No</td>
<td>17</td>
<td>22</td>
</tr>
</tbody>
</table>

Source: Primary Data

78 per cent of the companies have a separate hall for the board meeting. Only in some 22 per cent of the companies, a separate venue is not available within the registered office. This also indicates that most of the companies' board are effective boards.

4.6.4 Attendance

One of the most important attributes to evaluate the board room performance is the directors' attendance for the board meeting. The directors are the representatives of the shareholders. They are responsible for the management of the affairs of the company. The directors have the powers only collectively and not individually. The directors make the decisions through the meetings only. It is the vehicle through which they make decisions. Such meetings of the directors are known as Board Meeting. One of the factors for judging the directors' participation and involvement is regular attendance in the
board meeting or annual general meeting or any other committee meeting in which the director is a member.

Therefore, the attitude of the individual directors towards the boards can be gauged with the help the attendance records, both at the board meeting as well as annual general meeting. If a board member fails to attend frequently, his views cannot be heard. So the Companies Act is also serious regarding the attendance. However, the purpose is not served with the provisions of the concerned section. The section which deals with the attendance of the directors is section 283.

Under section 283 of the Companies Act, the office of a director shall become vacant under any of the following circumstances:

if he fails to obtain qualification shares required under the Articles within 2 months of his appointment as such or ceases to hold them at any time thereafter:

if he is found to be of unsound mind by a competent court;

if he applies to a Court to be adjudicated insolvent;

if he is adjudged to be an insolvent;

if he is convicted by a Court for moral turpitude and is sentenced to imprisonment for not less than six months;

if he fails to pay any call on shares, held by him, within six months from the last date fixed for its payments, unless the central Government has removed this disqualification by a Gazette notification;

if he absents himself from three consecutive meetings of the Board or from all meetings of the Board for a continuous period of three months, whichever is longer, without obtaining leave of absence from the Board. 20 It is the last condition that deserves one’s attention in the present context.

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20 Prasanta K. Ghosh, Textbook of Company Secretarial Practice, New Delhi, Sultan Chand & Sons
The period of three months is calculated from the date of first Board meeting from which the director absents himself. The word 'absents himself' imply voluntary or deliberate absence and do not cover cases of involuntary absence caused by illness etc. or by events beyond his control.21

The above section is not serious enough in compelling the directors' attendance for the board meeting. On the first occasion the act says that if a member fails to attend three consecutive meeting he has to vacate the office of the directorship. However, the explanation goes against the spirit of the original wordings. If the director deliberately did not attend the meeting, then only the section comes into effect. If the absence is not voluntary he need not be dropped from the board. The Act is silent, for how long a director can be away from the board meeting with the leave of absence. As pointed out earlier, that the board is only an old boys network. Therefore, many of the members of the board are either relatives or friends of the promoters as mentioned on earlier occasions. Therefore in the real life situation, the promoters gave those directors who were not present, leave of absence, even without any requisition for the sanction of leave of absence. At times, the minute book will be sent to the houses of directors who have not been able to attend the meeting in order to make them present in the board meeting.

Despite the blatant abuses, industry as well as the environment did little to rectify this situation. Neither the Companies Act nor SEBI did anything to rectify this situation. It is a serious matter. However, the same situation is effectively handled by SEC in the U.S.A., a counterpart of our SEBI. In 1978, the SEC initiated a request that the names of all directors who attended 75 per cent or less of all meetings be publicised. This is a trivial punishment for a serious misdemeanour, a shirking of duty. Though, in U.S. the corporate

21 Ibid
activists are not satisfied with the action initiated by the SEC, no such action is contemplated either in the frequently amended Companies Act or by SEBI.

Though the listing agreement compels a company to inform the stock exchanges the date of the board meeting and the purpose of the meeting, the attendance record of the individual director is still a confidential record. It has not yet become a public document. The records of the board meeting is assumed to be strictly a confidential matter. The irony is the fates of the companies’ performance are influenced by the board meetings, which in turn is influenced by the directors attendance. However, the legislators have not yet compelled the attendance records of directors in the board meeting.

PIRC, a British corporate governance activist organisation, has called for disclosure on director's attendance records. PIRC would like to see that a rule that is disclosing the names of the directors who have not attended 75 per cent or less of the board meetings is incorporated in the listing rules. Abbey National is one of the few UK companies to make a statement on this issue, providing a list of the number of board and board committee meetings attended by each director during the year. In India it is a distant dream, where the laws are still favourable to promoters.

The present researcher, though not in a position to obtain the statistics from the companies regarding the individual attendance particulars of the directors, collected the information regarding the number of board meetings conducted and average attendance for the board meeting for a period of five years has been solicited. The relevant question framed for that purpose is:

“Q.No:41. Details of Board Meeting conducted.”

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Board Meetings conducted</th>
<th>Percentage of average attendance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1992-93</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1993-94</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1994-95</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1995-96</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1996-97</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

22 PIRC calls for 'warts and all' detail PIRC Intelligence, March 1998.
Information pertaining to, number of board meetings conducted during the year and percentage of average attendance in the past five years, has been solicited. Hence the results could not be tabulated. The average number of board meetings conducted during the period 1992-93 to 1996-97 came to 4.96 and average attendance of the board members during that period is 85 per cent. To conclude and infer the effectiveness of the board from this angle, the board had performed in a better manner. 85 per cent of board room attendance is an appreciable one. Though the act or the listing agreement do not insist upon any minimum percentage for the directors, the average attendance of 85 speaks well about the directors involvement in their companies. Average number of board meetings is around 5, which is more than the stipulated statutory minimum of four meetings per annum. One can come to a judgement from this angle also, regarding the question how well a board functions.

The attendance of the directors’ has also been solicited through another question also, in order to validate the information obtained through question number 41. The relevant question is question number 12, the responses for the same has been recorded in Table 4.13.

“Q.No:12 Average Attendance in a Board Meeting (in percentage):”

<table>
<thead>
<tr>
<th>Table 4.13</th>
</tr>
</thead>
<tbody>
<tr>
<td>Board Attendance</td>
</tr>
<tr>
<td>Percentage of Attendance</td>
</tr>
<tr>
<td>--------------------------</td>
</tr>
<tr>
<td>70-80</td>
</tr>
<tr>
<td>80-90</td>
</tr>
<tr>
<td>90-100</td>
</tr>
</tbody>
</table>

Source : Primary Data

The response of the secretaries revealed that the average attendance of a board meeting works out to 85 per cent. The attendance record compares favourably well with the SEC recommendation of 75 per cent. The minimum level of attendance is 70 per cent and the maximum is 100 per cent, the median
level lies in the range of 80 – 90 per cent. Moreover, the information provided earlier for the question number 41 is also valid. The average attendance of the directors arrived as per the information given for both the questions work out 85 per cent.

4.6.5 Number of Board Meeting

The effectiveness of the board can also be judged by considering the number of board meetings conducted during the year. According to the provisions of the Companies Act, a company should conduct at least four meetings, each in a quarter. If the board happens to be a rubber stamp board or constitutional board, the company may convene only four meetings in order to satisfy the legal requirements. Therefore, to judge the board’s performance, information was solicited from the secretary by way of a question. The relevant question bears number 11. The question is:

“Q.No.11: Number of Board Meetings conducted during the year”

<table>
<thead>
<tr>
<th>Number of meetings</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>4</td>
<td>17</td>
<td>21.8%</td>
</tr>
<tr>
<td>5</td>
<td>45</td>
<td>57.7%</td>
</tr>
<tr>
<td>6</td>
<td>16</td>
<td>20.5%</td>
</tr>
</tbody>
</table>

Source : Primary Data

The average number of board meeting conducted per year worked out to 4.98, the median also was 5 meetings. Therefore one thing is clear, i.e., only 17 companies have treated the board meeting as a legal requirement. The remaining companies in the response group have used the mechanism of board meeting for the management of the company. Companies constituting 20.5 per cent met 6 times in a year. The conclusion is that the average number of the board meeting was 4.98 as compared to the responses of the question number 41,
viz., 4.96. Once again, the researcher has been convinced regarding the dependability of the information provided by the respondents.

4.6.6 Duration

Another factor which can be used to evaluate the performance of the board meeting is the duration of the board meeting. Longer the time devoted for the board meeting, more will be the effectiveness of the board meeting and vice-versa. Hence question number 10 was included in the questionnaire, to judge the performance of the board from this angle.

“Q.No:10. What is the normal duration of a Board Meeting?”

Table 4.15
Duration of the Board Meeting

<table>
<thead>
<tr>
<th>Time</th>
<th>No. of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Upto 1 Hour</td>
<td>52</td>
<td>66.67%</td>
</tr>
<tr>
<td>1 - 2 Hrs.</td>
<td>18</td>
<td>23.08%</td>
</tr>
<tr>
<td>More than 2 Hrs.</td>
<td>8</td>
<td>10.25%</td>
</tr>
</tbody>
</table>

Source : Primary Data

The responses showed clearly that the board meeting was held only for one hour in 52 companies, i.e., 66.67 per cent of the companies devoted one hour for the conduct of the board meeting. It does not speak well about the performance of the board meeting. It appears that they are treating it as a legal compulsion. We can take that majority of the boards belong to the constitutional type. It is interesting note down the observation of Mr. R.K. Talwar, former banker on the purpose of board meeting. “For what purpose are board meetings held? It is not a cynical view, but a portrayal of reality to say that the purpose is
more to meet the legal requirements than with the objective of involving the directors in decision making and securing policy guidelines”. 23

4.6.7 Minutes of Board Meeting

Every company is required to maintain the minutes of proceedings of every board meeting in a separate book. The proceedings of the meeting must be completed within 30 days of the meeting. There are three types of minutes books, viz., “Minutes of Resolutions”, “Minutes of Narration” and “Minutes of both”. The type of minutes book maintained by the company also indicates the nature of the board. If the company maintains a minutes of narration, the board is transparent. It is ready to record what is going on inside the room. Though it is not compulsory, to publish the contents of minutes book, still it is a documentary evidence which may be accepted as legal evidence. Therefore, the nature of the board is judged by the present researcher, by a question. The relevant question is:

“Q.21. The nature of the minute book for the Board Meeting maintained by the Company is (i) Minutes of Resolution (ii) Minutes of Narration (iii) Both”

<table>
<thead>
<tr>
<th>Types of minute books</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minutes of Resolution</td>
<td>43</td>
<td>55.12</td>
</tr>
<tr>
<td>Minutes of Narration</td>
<td>9</td>
<td>11.55</td>
</tr>
<tr>
<td>Both</td>
<td>26</td>
<td>33.33</td>
</tr>
</tbody>
</table>

Source: Primary Data

The responses to the question are tabulated in Table number 4.16, which shows that majority of the companies have been maintaining only minutes of narration. Nearly 55 per cent of the companies have maintained only minutes

of narration. In other words, they are not ready to even record what is happening inside the board.

4.7 ANNUAL GENERAL MEETING VIS-À-VIS DIRECTORS

The present legislation treats the board room attendance as a confidential matter. It is the discretion of the company to divulge any information regarding the attendance of the directors in the board meeting. However, the attendance records of the annual general meeting is more transparent and available. Moreover, annual general meeting is the vehicle through which directors are elected and inducted in the board. The directors are supposed to report to the annual general meeting about the company. Therefore, the directors have a moral duty to attend the annual general meeting, though there is no legal compulsion. Hence, one can also judge the attitude and involvement of the directors in the board process from the attendance records of the directors in the annual general meeting, apart from the attendance pertaining to the board meeting.

Therefore, the present researcher framed two questions to highlight the attendance records of the directors in the annual general meeting. One question is with respect to executive directors and another for the non-executive directors. Question number 52 solicits information for the executive directors. The relevant question is:

"Q.No:52. On an average how many executive-directors attended the AGM in the last 5 years?"

| Table 4.17 |
| Attendance of Executive Directors for the Annual General Meeting |
| Percentage of Executive Directors Attending the Meeting | Number of Companies | Percentage of Companies |
| Nil | 15 | 19 |
| Up to 50 | 60 | 77 |
| Above 50 and upto 100 | 03 | 4 |

Source: Primary Data
The responses to the above question were presented in table number 4.17. The responses indicate that in 63 companies, executive directors had the practice of attending the annual general meeting. 19 per cent of the companies did not compel the executive directors to attend the annual general meeting. Of the executive directors who attended the annual general meeting only 50 percentage of directors have had the practice of attending the annual general meeting. Only in 3 per cent of the companies more than 50 per cent of the directors have the practice of attending the annual general meeting. The same methodology was also extended to non-executive directors. Question number 53 was put to the companies’ secretaries. The relevant question is:

"Q.53. On an average how many Non-Executive directors attended the AGM in the last 5 years?"

Table 4.18

<table>
<thead>
<tr>
<th>Percentage of non-executive directors attending the meeting</th>
<th>Number of companies</th>
<th>Percentage of companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>50-60</td>
<td>07</td>
<td>09</td>
</tr>
<tr>
<td>60-70</td>
<td>19</td>
<td>24</td>
</tr>
<tr>
<td>70-80</td>
<td>16</td>
<td>21</td>
</tr>
<tr>
<td>80-90</td>
<td>09</td>
<td>11</td>
</tr>
<tr>
<td>90-100</td>
<td>27</td>
<td>35</td>
</tr>
</tbody>
</table>

Source : Primary Data

Table 4.18 shows the responses of the company secretaries regarding the attendance of the executive directors. It is encouraging to note that in 21 companies, 100 per cent of non-executive directors had the practice of attending the annual general meeting. It reveals that the directors have cared for the shareholders, and hence, they attended the shareholders meeting. However, in 54 per cent of the companies the directors’ attendance has been less than 80 percentage. It is to be condemned that the directors who are enjoying a number of perquisites apart from the allowance and commission, if any, are not mindful in attending the annual general meeting. The laws should be suitably amended
to make them attend annual general meeting. May be in the earlier days when the Companies Act was legislated, the available talents might be very much limited. Now with the increase in the available talents, attendance of both annual general meeting and board meeting should be a criterion for reappointment.

Admittedly, some of the aversion to attending annual meetings stems from the excessive length and boring content of too many meetings. Another factor which may be responsible for the poor attendance of the non-executive directors is more number of directorships. If the number of directorship is limited, the non-executive directors would have shown interest in attending the meeting. In the companies surveyed nearly 35 per cent of the companies have declared that the attendance percentage of the non-executive directors attending the annual general meeting has been in the range of 90-100. It is encouraging to have such huge attendance in as many as 35 companies. The main reason would have been lesser number of directorships.

One another reason may also be instrumental in the poor attendance record. In most of the companies, the non-executive directors are not eligible for any other remuneration, apart from sitting fees and travelling allowances. If one wants the non-executive directors to concentrate in the affairs of the company, then they have to be rewarded suitably. So far such posts are only ornamental posts. Hence they never consider it as a job. CEOs usually take care of the entire management, including strategic planning. Only as a legal requirement, many of the boards are functioning. If at all the Government wants to improve the functioning of the board, they have to suitably reward for the contribution, one normally expects from the directors.

There is one quotable incident, in Indian corporate history, where the entire management team did not turn up for the annual general meeting, and as a result, the dissatisfied shareholders passed resolutions recommending the dissolution of the original board and requesting the Government to constitute a
new board. This incident has been recorded in the annual general meeting of Ralliwolf Industries. This is an exceptional case. Normally, chairman and CEO will be present in most of the companies' annual general meetings.

To evaluate the interest of the CEOs in the annual general meeting a question was included in the questionnaire. The question number is 51. The relevant question is:

Q.No:51. Had the CEO attended all the AGMs conducted during the last five years?

The secretaries of the companies responded negatively for 17 companies i.e., 22 per cent of the companies surveyed. 22 per cent of the CEOs stayed away from the annual general meeting. The remaining 78 per cent of the CEOs attended all the annual general meetings. The responses of the secretaries revealed that most of the CEOs have attended the annual general meeting. Still the absence of the CEOs cannot be lightly taken into account. The shareholders entrusted the business of running the company to the board. In turn the board vested the rights of the management with the CEO. If such CEOs do not turn up in the annual general meeting, where their masters are all present to evaluate the performance of the management, it is a great insult to the shareholders. The law should make the attendance of the CEOs compulsory. The dates of the annual general meeting is normally fixed by the CEO and other members of the board. In spite of the fact, if a CEO is absent in the annual general meeting, it cannot be digested. It shows that such CEO has lightly taken the business of annual general meeting. It is the basis of his existence as CEO. Fortunately, only some 22 per cent of the CEOs have not attended the annual general meeting.

However, the attendance of the directors as well as CEO should be made compulsory at least for the annual general meeting, as they have accepted the assignment of directorship. Similarly, the directors should also be suitably rewarded for that responsibility. The present practice is that in most of the
companies the directors especially the non-executive directors are eligibly only for the sitting fees which is very meagre and nominal for their stature and position. Therefore, if such compulsion is made, no bidders may be available for the post of directors. Similarly, the executive directors should also be compelled to attend all the annual general meetings. For this, the company law should be suitably amended.

Yet another reason for the poor attendance is the irritation at the meetings 'turned into circuses' by chronic disrupters. Gadflies are one of the reasons for the poor attendance records. The promoters have been accustomed to be in the midst of 'yes sir' group. If they have been forced to be in the midst of numerous and embarrassing questions, all of a sudden, really it becomes a tough job emotionally. They may not be able to tolerate and digest such behaviour from an erstwhile docile group of people. Hence the poor attendance record of non-executive directors.

Yet staying away from an annual meeting simply to avoid gadfly confrontation is not the only excuse; outside directors have other excuses. Some complain that the meetings are too long, and others feel their meetings are so brief that it is a waste of time and money to attend.

4.8 NATURE OF A BOARD

Whenever one of the "scandals" breaks, the board's failure is blamed on stupidity, negligence of board members, or on failure of management to keep its board informed. But when such malfunction occurs with unfailing regularity, one must conclude that it is the institution that fails to perform rather than individuals. The board, whatever is name and whatever its legal structure, has become a fiction. The law may still treat it as the sovereign organ of the corporation. The reality, however, is that the boards are either simply management committees, or they are ineffectual. Rather than decrying the
failure of individuals, it is better to explore “Why have boards, regardless of
their legal structure, lost their capacity to perform?”

The history is replete with a number of examples where the same model
has contributed considerably in the beginning. If in the earlier days they did
perform, why not now? One reason for the malfunction of the board is, of
course, the development of the large publicly held companies. The original
board, whether American, English, French, German or Indian, was conceived as
representing the owners. This was reality in the past, when stock ownership, by
and large, was concentrated among a few people or a few groups, each holding a
substantial share of the total. Each board member had a sizeable stake in the
enterprise. Each was able to devote a good deal of time and attention to the
company. Each sat on only a few boards.

However, to-day’s boards nature is totally different. The large
companies are no longer owned by a small group. Their legal ownership is held
by several thousands of “investors”. The ownership is profusely diffused. The
boards no longer represent the owner, or indeed anyone in particular. As a
result, board membership has lost its rationale. People are invited to sit on
boards because of their name. Or worse, board members are recruited from
people who do business with a company, such as the company’s bankers or the
company’s lawyers. Above all, board members are being recruited from among
successful corporate executives. There was a report in the media, at one time,
that “Mr Dadiseth, former chairman of HLL, will be accommodated in the Tisco
board. However, the rules of HLL will not permit him to accept the external
directorship. But once Mr Dadiseth became the director of Unilever, the
chances of Mr. Dadiseth accepting the directorship in TISCO is becoming bright
as the rules of Unilever is different from that of HLL”. 24 Therefore, the
criterion for selecting a candidate for the board is either he should be related to

the promoters or friends or popular personality known to the public. If the directors are recruited with this criterion, performance may not be good.

Another factor is that the board cannot be what the law in most countries says it should be. It cannot be the governing body of the company. That is a full-time job. To try to do it on a part-time basis means that only trivia will even be looked at, let alone discussed. A final factor in the steady decline of the board has surely been that top management, by and large, does not want a really effective board. And this, to most top management appears to be a restraint, a limitation, an interference with management prerogatives, and altogether a threat. As a result, in Germany, the members of the supervisory board, which are supposed to supervise the second-tier board structure viz., management board, are hand picked by the chairman of the management board. Institutions give due weightage to such suggestions. Therefore, whether one follows Anglo-American Model or German Model, management has an upper hand than the board. Though they are at the second tier level they have the natural advantage because of their position.

Many top management will argue that there is nothing wrong with the decline of the board. They are perfectly contend to see the board become a legal fiction. Indeed they would be perfectly willing to see the board disappear altogether (and where the board is completely an "inside" board, that is, controlled entirely by members of top management, the board as such has disappeared). But this is exceedingly short sighted. It is becoming increasingly clear that top management will not—and in the large corporation must not—be permitted to operate without an effective and strong board. The alternative to top management’s developing an effective board for its own needs and those of the enterprise, is the imposition by society of the wrong kind of board, especially on the large corporation. Such an imposed board will attempt to control top

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management and to dictate direction and decision. It will indeed become the "boss". It must consider itself an adversary of top management. It will not, indeed, cannot, act in the interest of the enterprise. The first signs of this are clearly around us – indeed, it may already be too late to reverse the trend.

The malfunction of the board first became apparent in the Germany of the Weimar Republic. And it is in Germany where the first outside control has been imposed on the boards of large companies, in the form of “co-determination”, that is, of legally required worker representation on the board, first for companies in the coal and steel industries and then for all large businesses. Of course, no worker representative sits on German company boards; the members are trade union officials. But this does not alter the fact that the large-company board in Germany today has become a battleground for contending factions.

In the United States, in the last few years there has been mounting pressure to make boards “relevant”, that is, to appoint as board members representatives of all kinds of groups: Blacks, women, the poor, and so on. These appointees, no matter how distinguished the individual, cannot function as board members. Their role is to represent this or that outside group, this or that special interest. Their role must be to make demands on top management and to push special projects, special needs, and special policies. They are not concerned with, or responsible for, the enterprise. Nor should they be expected to hold in confidence what they hear at board meetings. In fact their allegiance is not to the enterprise but to their constituents outside. These developments demonstrate that society will not allow top management to exercise its power without an appropriate and effective board. The board, as it has been conceived originally – well over a century ago – has indeed outlived its usefulness. This, however, makes it an urgent top-management job to think through what kind of a

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27 Ibid.
board the enterprise should have. The decay of the traditional board has created a vacuum. It will not and should not remain unfilled. As Aristotle puts it, Nature abhors vacuum.

The Indian version of the board with respect to the representatives of various sectors of the society is still in the evolutionary stage. The Government inserted a provision in the Companies Act to enable representation to small shareholders. Though it is enacted, still the Government has to finalise the modus operandi for the same. Now doubt prevails over the implementation of the provision. However, it is a representation only to the owners and not other constituents. There is a powerful lobby against such representation to small shareholders. If that is the case, one need not doubt about the representation to other constituents. Regarding representation to other constituents as in U.S.A., there is no legal compulsion. The researcher to ascertain the prevailing condition in India constructed a questionnaire. The relevant question bears number 6.

"Q.No:6. How many directors are in the Board
(a) Number of Executive Directors : 
(b) Number of Non-Executive Directors : 
(c) Number of Nominee Directors : 
(d) Number of Labour Representatives : 
(e) Number of Independent Directors :"

The survey results revealed that no company had representatives even from the labour side. However, from the functioning point of view, representation from different groups like labour, different community, women etc will spoil the broth. The purpose of the board will be defeated. May be in the American context, representation might have been given importance. Moreover, after having satisfied the requirement of the shareholders, the society would have demanded more from the company. However, the prevailing position in India is totally different. Here, shareholders have to fight even for demanding their basic rights. The main correspondence between a company

28 Ibid
and a shareholders is only for getting his shares transferred. In many cases they have to approach the court of law even for getting their shares transferred in their name. Copious correspondence is initiated by the shareholders for getting the lost dividend warrant since the company is not properly responding to the shareholders. Under such situations, one cannot demand or even expect, a company to satisfy the aspirations of the other sections of the community.

4.8.1 Size of the Board

What should be the optimum size of the board? According to section 259 of the Companies Act, 1956, the minimum strength of the board is 5 in the case of a public limited company and the maximum is 12. However, this can be increased even beyond twelve with the approval of the Central Government. The size of the board depends on the size of the company, its turnover, complexities of business and nature of operations. The size of the board differs from company to company. Although no theoretical work exists on the optimal size of the boards smaller boards result in less free riding and promote more rapid decision making. To ascertain the position prevailing in India the researcher solicited information through a question. The relevant question is bearing number 6, has been reproduced above. The responses revealed that the average number of directors in the board is 7.9. The minimum is 6 with a maximum of 12. However, the median also happens to be 6 directors in the boards of listed companies in Tamil Nadu. In Pakistan, the maximum number for public companies varies from company to company, with most companies having 7 to 10 directors. In U.S.A., the average board size is 14. 29

29 William C.Frederick, Keith Davis and James E.Post, Business and Society, Singapore, Mc Graw Hill Book Company.
Table 4.19

<table>
<thead>
<tr>
<th>Total Number of Directors</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of Directors</td>
</tr>
<tr>
<td>---</td>
</tr>
<tr>
<td>6</td>
</tr>
<tr>
<td>7</td>
</tr>
<tr>
<td>8</td>
</tr>
<tr>
<td>9</td>
</tr>
<tr>
<td>10</td>
</tr>
<tr>
<td>11</td>
</tr>
<tr>
<td>12</td>
</tr>
</tbody>
</table>

Source: Primary Data

4.8.2 Inside Director vs. Outside Director

The Board of the company evolves strategy and reports back to shareholders on performance. But that is not all. Between these two ends, lies the Board’s most important task – to become the pivot, steering, supporting and supervising people to translate strategy into action. Companies Boards have received close scrutiny and notice because of the general perception that they neither display enough enterprise, nor do they provide proper support to people in implementing action-plans. The key imperative before the Board is to be demonstrably effective in improving shareholder value, and being transparently accountable to all those on whom the company has any impact. The different codes all over the world and, now in India, have prescribed guidelines to help the Board shoulder this responsibility. However, these cannot be general remedies – eventually companies have to evolve a structure and system specific to their needs.  

Therefore, the study of corporate governance is incomplete without the study of the composition of the Board of Directors i.e. inside or outside directors. However, in Indian context, the more popular terminology is executive directors and non-executive directors. Insiders are board members who

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30 K.B. Dadiseth, Chairman, Hindustan Lever Ltd., “Corporate Governance In India”, 32nd A.D. Shroff Memorial Lecture delivered under the auspices of the Forum of Free Enterprise.
are on the company payroll with some operational responsibility. Consequently, they are sometimes referred as "functional", "employee", "management", or "officer" directors – they are also known as "full-time", "active", or "working" directors. In the Companies Act, 1956 they are also referred to as Whole-time Directors. In British terminology, they are called Executive Directors. Since they are full-time employees, Executive Directors are usually available for all board meetings, both regular and special. As a rule, inside directors do not receive any additional compensation for board or board committee services. Except for retired CEOs, their tenure usually ceases when they leave the company's employment.

Another category of inside director (and at one time the most important) is the owner-director, or his close relative. One of the features of corporate set up is the divorce between the management and owners. Therefore, in companies where the promoters are not able to occupy the seat of CEO, the promoters appoint their representatives in the board. In several hundred thousand first-generation owner-entrepreneur firms stock ownership is the prime factor in structuring the board.

Historically, inside directors are the legacy of strong company owner-founders who elevated the top executive group from "hired-hands" status to that of policy makers. Their long tenure and dedication to specific chores give them an unparalleled competency plus a high loyalty quotient. In short, inside directors tend to have the following characteristics:

- Superior pertinent technical backgrounds.
- Demonstrated leadership ability through long service in the company.
- Immediate availability for both routine and emergency sessions.
- Complete dedication to the organisation
- A keener comprehension of the wants and attitudes of the company's rank and file, shareholders, the customers, and their management colleagues.
At the other end of confusing continuum are the outside directors – also known as “non-management”, “non-employee”, “part-time”, “honorific”, “independent”, non-executive directors or “professional” directors. The outside directors will not be in the pay roll of the company. It is assumed that their separation from the company and its routine problems gives them a measure of superiority. Among the more frequently listed advantages of outside directors are that they:

- provide independent assessments.
- have broader backgrounds
- are more representatives of stockholders and society.
- give the best in checks and balances.

Non-executive directors can bring contestability within the board room provided they are independent and competent. Independence is partly a matter of character, which cannot be the subject of rules or codes. However, independence can be fostered inter-alia by avoiding commercial and personal relationships that can affect objectivity. A distinction should be made between connected directors and independent directors. The role of the latter should be clearly specified. If the function is clear and agreed then it avoids reliance upon individual assertion to resolve problems.

The factor of competency can be judged by the role played by the non-executive directors. They are supposed to play the role of systematic monitoring by challenging knowledgeably, incisively and fearlessly the actions and judgements of executives. In a recent (1994) survey in U.K., the roles of non-executive directors in protecting the shareholders interests and as custodian of good corporate governance were rated much higher in terms of importance as compared to their contribution to strategy and objectives based on industrial and commercial experience.

A question arises as to the nature of the functions to be performed by the non-executive directors. Is it to be restricted to contribute to the strategic direction of the company or to monitor performance and conduct of the
executive management or both? Non-executives as a body are clearly expected to perform both functions. However, it is questionable whether one individual can always do both. Monitoring performance and conduct of the executive management requires an element of independence, which not all non-executives will have.

However, overall within the board as a body, both functions are vital and inter-related. One is implied in the other. Non-executive cannot contribute to the strategic direction of the company if they do not effectively monitor the performance and conduct of the executive management. Non-executives must be in a position to communicate with shareholders if there are specific concerns. In this context, it of vital importance that shareholders' approval is required for the removal of a director, and vote with dismay that many companies have introduced a power which allows the directors to remove one of their number without recourse to shareholders.

The American Institute of Management has persistently lauded the superiority of outside directors over inside directors. In one of its earlier issues of the Manual of Excellent Management the AIM makes a profession of faith. "One of the fundamental tenets of the Institute is that the majority of the members of any board should be drawn from outside the company. This is, the Institute is convinced, the only means whereby objectivity in approach and clear-cut decisions on corporate problems can be assured. Companies which are rated excellent in this category, but who do not fulfil this requirement, are excellent despite the condition." Again, the conclusion of the institute, that the majority of the board should be drawn from outside the company so that objectivity in approach and clear-cut decisions can be assured, is conditional. The way in which such outside directors are selected, the criteria followed in such selection, competence of such outside directors is the ultimate factor to conclude that the best decisions can be assured.
The Cadbury Committee has recommended a very important role for non-executive directors. The code of best practices set out by the committee states “Non-executive directors should bring an independent judgement to bear on issues of strategy, performance, resources including key appointments and standards of conduct”. Though there is a high expectation from this institution to contribute towards the organisational objectives, in reality their role playing is subject to a number of criticisms. It is difficult to expect these non-executives to play a key-role in protecting the shareholders’ interest. Often the competence of non-executives is questioned. While top management experience or excellent professional attainments might be the best career background for a non-executive director, these may not be the ideal background for the corporate governance role. There is another genuine risk in assigning the specific task of monitoring to the non-executive directors. This has the potential for board-room split. In case non-executive directors are perceived as ‘board-room policeman’, they may not get all the information on what executives are doing. Moreover, their presence in the board room might stifle the entrepreneurship zeal of the managers and they might become reluctant to take even reasonable business risks. The danger of insiders trading and corporate-espionage can not be ruled out. In the U.K. – survey referred to earlier, most of the executives expressed the opinion that the non-executive directors should not have access to ‘price-sensitive’ information. The high-expectations from non-executive directors might be logical but the issues involved are complex. The crucial questions are whether executives would be interested to be watched in the board room and how to motivate mature and accomplished professionals with high business acumen and integrity to join boards of companies and to effectively contribute in improving corporate governance.

In a pioneer study of 200 major industrial corporations between 1925 and 1950 in the U.S.A., the composite firms with distinctly inside boards

unquestionably outperformed those with predominantly outside boards, while the companies with mixed or “hybrid” boards had an intermediate performance record. Again, the inside- or officer-director boards were found to be superior in a latter study during 1963. This follow-up study did, however, show that the ratio of inside to outside directors had begun to shift somewhat in favour of outsiders. No such studies are available in India to establish the superiority of either executive directors or non-executive directors in the Indian context. Though the corporate history dates back to 19th century, till independence, the scene is more dominated by British merchants and some Indian business men. Both the British merchants as well as Indian business men used managing agency system. Hence the institution of directors is not permitted to have the normal growth. The growth is stifled.

In spite of the problem to be faced by the non-executive directors, with the increase in the number of directorships, the momentum is increasing for the appointment of more number of non-executive directors. It is now firmly established that non-executive directors are essential to corporate governance and they can and should make a powerful contribution to the development of the corporation. By bringing their different and often extensive experience, they provide valuable support to the management. They also see to that the rights of shareholders and other stakeholders are ensured and that the company observes high standards of corporate governance. According to a recent study by Ernst and Young, the consensus was that the main function of a non-executive director is to “provide strategic input the board level. They add value of bringing moderation and balance to strategic decisions and help create healthy board dynamics.” To ensure independence of judgement, the non-executive directors should be independent of the company and have no affiliations with the sponsors or their associated companies.

However, because of the legal issue, many people are reluctant now-a-days, to accept the posts of non-executive directors. The reason being the legal responsibility of non-executive directors. The existing law does not make a distinction between executive directors and non-executive directors in terms of liability notices for operational and other irregularities are issued to all directors. This discourages many professionals to join boards of companies as non-executive directors. It is argued that though non-executive directors have fiduciary responsibilities, they should not be held responsible for operational deficiencies because they are not in day-to-day charge of managing the company.

The institution of board evolved in order to satisfy the legal requirement. At the evolutionary stage, the promoters filled the board with their relatives and friends. Gradually the financiers and other advisors were also accommodated. At one stage, the paid employees of companies were also accommodated in order to reach the minimum number of persons as stipulated in the act. Of late an increasing number of retiring company top executives, public figures, government officials, and university government officials, and university presidents now seek post retirement careers as outside or professional directors. Note that the designation “professional” is used in a wide variety of senses, but generally it refers to an outside director who makes a living by serving on a number of boards. Obviously, the living-off of directorate fees can be quite comfortable. A commonly quoted statement is Lord Boothby’s sentiments on his own “eight or nine” directorships – explaining what he and his British peers serving as outside directors do in adding prestige to corporate letter hands: “No effort of any kind is called for. You go to a meeting once a month in a car supplied by the company. You look both grave and sage, and on two occasions say ‘I agree,’ say ‘I don’t think so’ once, and if all goes well, you get $ 1,440 a
year. If you have five of them, it is total heaven, like having a permanent hot bath." This is the position which was prevailing in U.K.

Industrial elitism in the form of old boy networks is not exclusively an Indian phenomenon. It was in prevalence throughout the world, right from the beginning of the corporate history. After World War II, when the German aristocracy was displaced, there arose a new hierarchical top-level Geldaristokratie, the industrial plutocracy. Thousands of blue bloods now found a new sinecure. “The boards of big industrial companies are liberally studded with noble names. The names are particularly in demand as public relations men. “I do like snobs” exclaims one princely P.R. man. “They are all so kind to one. All you need to get ahead in industry is reasonably good looks, self-assurance and organisational talent. This the nobility had, and now the young ones are all fat people in their firms.”

In the United States, old boy networks are not so much a function of aristocracy as they are of plutocracy – control by moneyed interests. Yet there is a congenital propensity among successful businessmen to found dynasties.

Interestingly, there is no evidence to show that corporate boards cluttered with prestigious personages have been particularly effective. In fact, some negative relationships might come about because these prominent outsiders have other more pressing demands. “In the past some directors particularly notables ‘who look good on the roster,’ according to one businessman – often skipped meetings. Ellsworth Bunker, the U.S. Ambassador to South Vietnam, has been a director of Curtis Publishing Company since 1963. But he attended only one board meeting in a period of two years, a Curtis spokesman says.”

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India is not a land of exception. In the earlier days, the companies were started, funded and run by the promoters. Boards were packed with friends and relatives. Subsequently as the promoters start more and more number of companies, the limitation on the number of directorships an individual can accept compelled the promoters to follow another strategy, viz., filling up the boards with retired judges, retired Executives of public sector enterprises and bureaucrats. The practice of filling the boards with retired Government employees reached the peak in the mid nineties. The new breed of promoters who entered the market for the first time, relied upon and impressed by the names of ex-employees of Government and public sector enterprises. In fact the judges, executives of public sector enterprises, became the victims of dishonest promoters. The new promoters in order to woo the public, they convinced the popular public personalities to accept directorship. As far the retired personnel are concerned, such posts are ornamental posts. Without realising the vicarious designs of the promoters, many people have lent their names and subsequently they are in trouble. Indian shareholders are not so active as in U.S. or U.K., else such public figures have to stand in the court of law. One or two such cases can also be cited in India where the heroes of yesteryears are now in the corridors of the court in connection with such directorships.

The institution of executive directors and non-executive directors are common only in the countries where they are following the unitary board model. Where two-tier structure is in use, upper tier known as supervisory board and lower tier known as management board, the two boards are water tight compartments. The management committee members are full time employees of the company. The members of the supervisory boards are restricted to be a member in the management board. Dual membership is prohibited. All the members of the supervisory board are non-executive directors. Similarly all the members of the management board are executive directors. Hence the usage of executive directors and non-executive directors is not popular, where the two tier
model is followed. U.S. and UK boards are typically unitary board type. They consist of both inside officers and outsiders, while Japanese boards are composed entirely of insiders. Some of the countries, where executive directors as well as non-executive directors are permitted to take the seat in the board are countries like Singapore, Canada etc.

The board should be well-balanced, with experience and ownership represented. It should be so balanced between executive and non-executive directors so that no individual or group would be able to dominate. The Hamphel Committee suggests that a typical board should have a balance of executive Directors and non-executive Directors (including independent non-executives) such that no individual or small group of individuals can dominate the board’s decision-making. The modern trend is to have lesser number of inside directors, who represent family members of family-owned businesses, and more independent, non-executive directors. As observed earlier Indian corporate law is more in alignment with British corporate law. However, there are certain cosmetic differences between the Indian version and Britain version. The differences are the result of the differences in socio-economic-political conditions prevailed in both the countries. One such difference between British board and Indian board is that there is no difference between executive and non-executive directors in Indian boards as in the case of British version. There is no such species as Executive Directors and Non-Executive Directors in the Indian Companies Act, 1956 or even in earlier versions. At the time of framing the Companies Acts, the available talent in the country was too much limited. Perhaps this might have lead the legislators to bifurcate the institution of directors into Executive Directors and Non-Executive Directors.


The Indian version of this issue is slightly different, with some cosmetic difference. The Indian Companies Act, provides only for a unitary board. Therefore, there is no restriction for dual membership. However, there is no mention about executive directors and non-executive directors in the Companies Act. It provides for different types of directors like rotational, whole-time or managing directors alternate directors etc. However, the closely related terms to the current issue that is under discussion is whole-time director and managing director. The term whole-time director is not defined in the Companies Act. According to section 269 of the Companies Act, 1956 a company must appoint either a Managing Director or Whole-time Director or a Manager as the second agency of the management to look after the day-to-day management of its affairs. The term whole-time director and managing director is not defined in the Companies Act. Both are basically executive directors. Both are inside directors with managerial responsibility. Other types of directors mentioned in the act are from other angles. It is not related to the issue of inside or outside director. Rotational director is one who automatically retires after three years and seek his re-election. Similarly the term alternate director refers to an individual who will be acting as a substitute for a director. Section 313 envisages the appointment of an alternate director to act for a director during his absence in India for a period of not less than three months.

The managing director acts as the CEO of a company with substantial powers of the management. The managing director is usually appointed under a service agreement. Hence, he is both a director as well as an employee. A managing director can be appointed for a term of five years only concurrent with his continuing as a director and must seek appointment thereafter. Similarly the term whole-time director is a person who is in whole-time employment of the company. He carries out the function of a managing director. The executive control is in the hands of whole-time and managing directors. Further, an individual can occupy a seat in the board and also be a member of the
management team. Dual membership is permitted. In the terminology of English Corporate Law the executive directors are one, who are in the board as well as a member of the management team, compared to a non-executive directors who are the members of the board only.

In order to ascertain the situation in Tamil Nadu, the researcher has incorporated two questions in the questionnaire. Question number 6 has been already reproduced in the above paragraphs. The responses to the question number 6 were tabulated in Table number 4.19 to 4.22. It reveals that no companies surveyed have labour representatives as well as alternate directors. In general non-executive directors dominates a board. The average number of executive directors per company is 1.8 and the statistics for the non-executive directors is 5.33. This clearly highlights that the companies in Tamil Nadu have had boards dominated by non-executive directors. Similarly, the independent directors are in the board only in 23 companies whereas only 17 companies have nominee directors in the board.

Table 4.20
Board Composition

<table>
<thead>
<tr>
<th>Type of Directors</th>
<th>Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Executive Directors</td>
<td>1.8</td>
</tr>
<tr>
<td>Non-Executive Directors</td>
<td>5.33</td>
</tr>
<tr>
<td>Alternative Directors</td>
<td>Nil</td>
</tr>
<tr>
<td>Labour Representatives</td>
<td>Nil</td>
</tr>
<tr>
<td>Independent Directors</td>
<td>0.46</td>
</tr>
<tr>
<td>Nominee Directors</td>
<td>0.12</td>
</tr>
<tr>
<td>Overall average</td>
<td>7.9</td>
</tr>
</tbody>
</table>

Source: Primary Data

Table 4.20 portrays the position of executive directors. Of the companies surveyed, 18 companies did not have any executive directors in their board. No company among the companies surveyed has more than 6 executive directors. The median for this type of directors is 2 and the arithmetic mean is 1.8.
Table 4.21

Executive Directors

<table>
<thead>
<tr>
<th>No. of Directors</th>
<th>No. of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nil</td>
<td>18</td>
</tr>
<tr>
<td>1-3</td>
<td>51</td>
</tr>
<tr>
<td>4-6</td>
<td>9</td>
</tr>
<tr>
<td>7-9</td>
<td>Nil</td>
</tr>
<tr>
<td>9 and above</td>
<td>Nil</td>
</tr>
</tbody>
</table>

Source: Primary Data

The present researcher has framed a hypothesis with reference to the executive directors. The hypothesis is that the average number of executive directors in the listed companies of Tamil Nadu is 3. In order to test the hypothesis, the researcher has applied Z test and applied the following statistical procedures:

Null Hypothesis:

There is no difference between the population mean and the sample mean.

Alternate Hypothesis:

The sample mean is not equal to population mean.

Level of Significance: 5%

Critical Value: 1.96

Calculated Value: 1

The results revealed that the null hypothesis can be accepted, as the calculated value is 1 and lies in the acceptance region. Therefore, the researcher establishes that the average number of executive directors in the listed companies of Tamil Nadu is 3.

Table 4.21 portrays the position of non-executive directors in the listed companies of Tamil Nadu. The arithmetic mean of non-executive directors is
5.33 and median is 6. All the companies surveyed had the institution of non-executive directors in their board.

Table 4.22

<table>
<thead>
<tr>
<th>No. of Directors</th>
<th>No. of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nil</td>
<td>0</td>
</tr>
<tr>
<td>1-3</td>
<td>17</td>
</tr>
<tr>
<td>4-6</td>
<td>44</td>
</tr>
<tr>
<td>7-9</td>
<td>8</td>
</tr>
<tr>
<td>9 and above</td>
<td>8</td>
</tr>
</tbody>
</table>

Source: Primary Data

The present researcher has constructed a hypothesis to test the average number of non-executive directors in the listed companies of Tamil Nadu. The hypothesis is that the average number of non-executive directors in the listed companies of Tamil Nadu is 5. To test this hypothesis the researcher has applied Z test and followed the following statistical procedures.

Null Hypothesis:

There is no difference between the population mean and the sample mean.

Alternate Hypothesis:

The sample mean is different from the population mean.

Level of Significance: 5%

Critical Value: 1.96

Calculated Value: 0.1

Since the calculated value lies in the acceptance region, the null hypothesis is accepted and alternate hypothesis is rejected. Since the hypothesis is statistically tested, the researcher concludes that the average number of directors in the listed companies of Tamil Nadu is 5. Further the above analysis
clearly shows that the institution of non-executive directors numerically dominates the corporate boards in Tamil Nadu.

It is interesting to note that the "Desirable corporate governance in India – A Code", released by CII that 30 per cent of the board should be constituted by accommodating non-executive directors, if the chairman of the company is a non-executive director. If the chairman happens to be the managing director also, 50 per cent of the board representation should be given to non-executive directors. Such non-executive directors should be professionally competent persons. The CII suggestions are applicable for a company with a turnover of more than 100 crores. The average size of the board of the listed companies in Tamil Nadu is 7.9. The average number of non-executive directors is 5. Therefore, the listed companies of Tamil Nadu satisfies the condition levied by the CII, that the proportion of non-executive directors to the total number of director is more than 50 per cent.

The Birla Committee, on the composition of the board, recommends that a company should have an optimum combination of executive and non-executive directors with not less than fifty per cent of the board comprising the non-executive directors. In case a company has a non-executive chairman, at least one-third of the board should comprise of independent directors and in case a company has an executive chairman, at least half of the board should be independent. This is a mandatory recommendation.

Generally, there is a feeling among the corporate observers that the executive directors are the officials appointed by the promoters or incumbent management. Hence they cannot be objective as well as reactive. They will be more submissive. Therefore there is a general consensus that the board should consist of more number of non-executive directors. The reservation over the institution of executive directors led the CII to stipulate a percentage of the board to be in the form of non-executive directors. As a result, in the CII Code of Desirable corporate governance, it recommended that 30 per cent of the board
should be constituted by accommodating non-executive directors, if the chairman of the company is a non-executive director. If the chairman happens to be the managing director also, 50 per cent of the board representation should be given to non-executive directors. Non-executive directors can bring contestability within the boardroom.

However, the institution of non-executive directors is also not free from charges. The non-executive directors are an asset for the institution provided they are independent. There is a general charge against the institution of non-executive directors that they are recruited from the old boys network of the promoters. Hence they cannot be as objective as they are expected to be. The position of the directorship is a gift of the promoters to such persons. Hence, such persons cannot and will not ask questions which are embarrassing to the promoters. In short they lack independence. Therefore it is doubtful for them to contribute effectively in the process of board functioning.

4.8.2.1 Participation

Therefore the researcher has decided to assess the performance of both executive directors as well as non-executive directors of the companies taken for the present study. The present researcher has constructed a question to ascertain how the executive directors participate in the board functioning. Since the executive directors are also employees, the level of participation may vary from that of the non-executive directors. Hence the following question number 32 in the questionnaire.

"Q.32. Executive directors' participation in the Board Meeting are:
(i) Active (ii) Very Active (iii) Indifferent"
The responses to the above question have been presented in table number 4.23. The respondents' observation is that 67 per cent of the executive directors are actively participating in the board meeting process. The remaining 33 per cent are coming under the category of very active. Therefore, according to the secretaries of the companies, the executive directors are contributing well to the board meeting. No director from this category are found to be indifferent. That is natural as they are all paid employees. If at all such executive directors are indifferent, they may be related to the promoters. For the welfare of the family and not the company they will be maintained in the same capacity. Fortunately in the companies taken as sample, no directors were indifferent.

One of the charges against non-executive directors is they are recruited from the promoters' old boys network or relatives. However, this point alone cannot invalidate such candidate. it has to be proved that the non-executive directors are not contributing to the process of the effective functioning of the board. To ascertain their level of contribution, a question similar to the question number 32 was framed from the point of view of non-executive directors. The relevant question is:

"Q.33. Non-Executive directors' participation in the Board Meeting are:
(i) Active          (ii) Very Active    (iii) Indifferent"
Table 4.24
Non-Executive Directors’ Participation

<table>
<thead>
<tr>
<th>Level of Participation</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Active</td>
<td>61</td>
<td>78</td>
</tr>
<tr>
<td>Very Active</td>
<td>17</td>
<td>22</td>
</tr>
<tr>
<td>Indifferent</td>
<td>Nil</td>
<td>Nil</td>
</tr>
</tbody>
</table>

Source: Primary Data

The responses to the above question is presented in table number 4.24. As in the case executive directors no director is indifferent in the proceedings of the meeting. Majority of the directors are contributing effectively by actively participating in the proceedings of the meetings. 22 per cent of the directors are actively participating in the meeting, thereby disproving that recruitment from the old boys network is not good. The non-executive directors are also not in an indifferent mood while attending the board meeting as in the case of executive directors. While comparing the participation of executive directors and non-executive directors, the level of participation is more or less the same. 78 per cent of non-executive directors are actively participating whereas in the case of executive directors it is 67. Since the non-executive directors away from the scene, they are in a position to demand or seek more clarification and the purpose of the combination is justified as far as the listed companies in Tamil Nadu.

4.8.2.2 Attendance Record

Another yardstick to measure the contribution of directors in the process of board functioning and their involvement, is their attendance to the board meeting. To ascertain to what extent they skip or attend the board meeting, question number 35 and 36 is included in the questionnaire. Question 35 is to solicit information with reference to executive directors and 36 with reference to non-executive directors. The relevant questions are reproduced below:

“Q.35. Average percentage of attendance of Executive directors for the Board Meeting?
"Q.36. Average percentage of attendance of Non-Executive directors for the Board Meeting?"

The average percentage of attendance is 74.44 for executive directors compared to 87.78 for non-executive directors. The range of attendance varies between 65% to 100% for the executive directors compared to 72.5% - 95% for non-executive directors. In 35 companies – 45% of the total companies - all the executive directors used to attend the board meetings, whereas such level of attendance has not been noticeable from the species of non-executive directors. In 33.33 per cent of the companies none of the executive directors have attended the board meeting as compared to 12% in the case of non-executive directors.

4.8.2.3 Directors Related to Promoters

Beholden or affiliated directors are typical in Indian corporate boards, and so are personal friends and interlocking directorates. There are many instances where sons and daughters, and friends and relatives are packed in promoter controlled boards. Most of them do not know enough to contribute to the management of a company, while many do not even attend board meetings. The only silver lining is that in the case of second generation promoters, many are trying to get professional qualifications. Yet another question is set to find out that to what extent the board of listed companies in Tamil Nadu is loaded with the relatives of the promoters. The relevant question bears number 7.

"Q.7. How many directors are related to the promoter group among:
(a) Executive Directors 
(b) Non-Executive Directors"

Table 4.25 highlights the relationship of directors in the board to the promoters. The responses revealed that 56 per cent companies have executive directors related to promoters. However, the percentage of non-executive directors who are related to promoters has been even high. Nearly 90 per cent of the companies have promoters’ relatives as non-executive directors in the corporate boards.
Table 4.25

Directors related to Promoters

<table>
<thead>
<tr>
<th>Directors</th>
<th>No. of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Executive Directors</td>
<td>44</td>
<td>56</td>
</tr>
<tr>
<td>Non-Executive Directors</td>
<td>70</td>
<td>89.7</td>
</tr>
</tbody>
</table>

Source: Primary Data

Table 4.26 shows the position of executive directors vis-à-vis promoters' relatives. 34 companies surveyed had not given any representation to the relatives of the promoters in the board as executive directors. 32 companies have accommodated at least one director as executive directors in the board of the companies they have promoted. Therefore the overall picture demonstrates that the promoters have not given much importance to their relatives in the appointment of executive directors, while constituting the board. This point is further amplified by the fact that the average number of executive directors who are related to promoters is only 0.74, compared to 1.8, the overall average of executive directors per company.

Table 4.26

Executive Directors related to Promoters

<table>
<thead>
<tr>
<th>No. of Executive Directors</th>
<th>No. of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>34</td>
<td>44</td>
</tr>
<tr>
<td>1</td>
<td>32</td>
<td>41</td>
</tr>
<tr>
<td>2</td>
<td>10</td>
<td>12</td>
</tr>
<tr>
<td>3</td>
<td>02</td>
<td>03</td>
</tr>
</tbody>
</table>

Source: Primary Data
Table 4.27

Non-Executive Directors related to Promoters

<table>
<thead>
<tr>
<th>No. of Non Executive Directors</th>
<th>No. of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>8</td>
<td>10.3</td>
</tr>
<tr>
<td>1</td>
<td>20</td>
<td>25.6</td>
</tr>
<tr>
<td>2</td>
<td>34</td>
<td>43.5</td>
</tr>
<tr>
<td>3</td>
<td>12</td>
<td>15.4</td>
</tr>
<tr>
<td>4</td>
<td>4</td>
<td>5.2</td>
</tr>
</tbody>
</table>

Source: Primary Data

Only in 8 companies relatives of the promoters have not been accommodated in the board as non-executive directors, out of 78 companies surveyed. A clear picture emerges on going through the data collected that the promoters give importance to their relatives while constituting the board. As a result out of 78 companies surveyed, 70 had the relatives of the promoters as non-executive directors in the board. The average number of non-executive directors related to promoters is only 1.79 compared to 5.33 the overall average for non-executive directors. The average number of executive directors who are related to promoter’s group is 0.74 compared to 1.79 for non-executive directors.

The researcher concludes the issue of inside directors and outside directors with reference to listed companies in Tamil Nadu, that both species have been active in the board meeting. Regarding attendance, non-executive directors have had the practice of attending more number meetings than their counterparts, executive directors. Though the number of proposals filed by both, executive directors and non-executive directors is meagre, still non-executive directors file more number of proposals. In 23 per cent of the companies, the non-executive directors have the practice of filing the proposals, compared to only 13 per cent in the case of executive directors. More companies (88 per cent of the companies) have the species of non-executive directors who are related to promoters. The percentage of companies where the executive directors who are
related to promoters are only 45 per cent. Therefore one can draw the inference that the board's composition is numerically dominated by non-executive directors. Moreover, the promoters' representation is also high only through the non-executive directors. Therefore, it is crystal clear, that the board's composition is not loaded in favour of the promoters' relatives.

4.9 TRANSPARENCY

A typical board should be transparent as far as possible. Board of Directors is an agent of the promoters. The board reports about the company through the Annual Report. The conventional reporting medium is the annual report. It is considered to be the mouth piece of the board. It bridges the shareholders with the board. In the olden days, the promoters who run the companies will communicate with the shareholders only through the annual report. If at all any communication is there in between the management and the shareholders, it is only through the explanatory statement given for any business to be transacted in the extra-ordinary general meeting. Therefore, the degree of transparency of a board can be judged by the contents of the annual report. The secretaries of the companies were asked to give the information content of the annual report of the year 1993-94. The relevant item in the questionnaire bears 55, which has been reproduced below:

"Q.55. Which of the following information is provided in the Annual Report for the year 1993-94?
(i) Debt-Equity Ratio
(ii) Explanation for extraordinary Income
(iii) Explanation for extraordinary Expenses
(iv) Capacity utilisation
(v) EPS
(vi) Market Price (High & Low)
(vii) Market Price Chart for 1 year or More
(viii) Cash Flow Statement
(ix) Explanation in sudden change in profitability
(x) Accounting Policies
(xi) Any other Information: (Please specify)"
Table 4.28

Information Contents of the Annual Report

<table>
<thead>
<tr>
<th>Information</th>
<th>Number of Companies</th>
<th>Percentage of Cos</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt-Equity Ratio</td>
<td>29</td>
<td>37</td>
</tr>
<tr>
<td>Explanation for extraordinary Income</td>
<td>29</td>
<td>37</td>
</tr>
<tr>
<td>Explanation for extraordinary Expenses</td>
<td>35</td>
<td>45</td>
</tr>
<tr>
<td>Capacity utilisation</td>
<td>31</td>
<td>40</td>
</tr>
<tr>
<td>EPS</td>
<td>43</td>
<td>56</td>
</tr>
<tr>
<td>Market Price (High &amp; Low)</td>
<td>9</td>
<td>12</td>
</tr>
<tr>
<td>Cash Flow Statement</td>
<td>61</td>
<td>78</td>
</tr>
<tr>
<td>Explanation in sudden change in profitability</td>
<td>19</td>
<td>24</td>
</tr>
<tr>
<td>Accounting Policies</td>
<td>61</td>
<td>78</td>
</tr>
<tr>
<td>Any other Information</td>
<td>23</td>
<td>29</td>
</tr>
</tbody>
</table>

Source: Primary Data

Table 4.28 reveals the information contents of the annual reports of listed companies in Tamil Nadu. EPS is an important information which is eagerly awaited by the shareholders, other investors as well as other market participants. Though the information is hidden in the annual report, for investors with no accounting background may find it difficult to ascertain the information. Hence, the board, which is transparent will reveal EPS. Only 56 per cent of the respondents disclosed this information in their annual reports.

Market price of the share is yet another essential information for valuing the shares by using the technical analysis. Many shareholders are retaining the shares for a pretty long time. They may not be watching the price movement. Therefore it is necessary for the company to provide the data relating the movement of the prices of the company shares. The data collected from the survey revealed that only a meager 12 per cent of the respondent companies provided the data. This is an unsatisfactory performance from the point of view of transparency.
78 per cent of the respondent companies have disclosed the accounting policies. From this angle, we have to appreciate the respondent companies as more than 78 per cent of the companies are providing this valuable information. Majority of the companies (45 per cent) are eager to explain extra-ordinary expenses rather than extra-ordinary income (37 per cent).

Another important information which the companies skip is ‘explanation in sudden change in profitability’. It is shocking to note that only 24 per cent of the companies utilise the annual report to inform the shareholders about sudden changes in profitability. It is really a sorry state of affairs. The Board of Directors owes a fiduciary duty towards shareholders. However, they are not ready to reveal the maximum to the residual claimants of the company i.e., shareholders.

On going through the responses, one can come to a conclusion that still the companies are far behind the practices prevailing in the developed countries. However, when compared to the prevailing situation among the companies in India, the score of the respondent companies are satisfactory. There is no statutory obligation to disclose any one of the above information during 1993-94. The researcher has solicited the above information for the year 1993-94, so that the real intention of the board vis-à-vis transparency can be ascertained. The present day environment creates a legal compulsion to provide such data, hence the researcher specifically asked the companies to provide the data with reference the year 1993-94.

In addition to that, the board should inform the shareholders when some material events have taken place in the company. It is the duty of the board to inform the shareholders. However, in reality, the news have to percolate down the line to reach the shareholders through the media. The existing practice in India encourages insider trading. The usual practice is the management will disperse the information among their close circle. Subsequently the information will be shared with the analyst, a species in existence who will analyse the data
and report to the press. The shareholders, who have the proprietary over the information will be the last group to receive the information through the media. The promoters do not think that it is their responsibility to share the information, with the owners of the company. The shareholders come to about their companies only through the media after the occurrence of the events.

In the post globalisation era, the SEBI attempts to set aright this matter by issuing orders. As a result the companies are now compelled to disclose material events to the stock exchange, by virtue of the listing agreement. Consequently the situation has improved. If one goes through the journals and other communication media, one can come across more information about companies compared to the past. But the irony is that still it is half-backed. The companies have come forward to disclose as little as possible, just to satisfy the legal requirement. The contents of the disclosure just touches the peripheral issue.

Though the companies are coming out with some information in the last three years down the line, the depth and breadth of information provided to satisfy the legal compulsion continues to be poor. ‘Just say the bare minimum’, seems to be the order of the day, with, perhaps, a few exceptions. The disclosures do not even explain the implications of a price-sensitive development. This is an almost universal trend, barring a few companies such as Infosys Technologies and HDFC. The end result is that the disclosure requirement has had limited use. The only thing in its favour is that even if the disclosures is delayed, or sketchy in discussing the implications of a certain development, an investor need not go through a variety of news sources to discover what corporate action is taking place.

Poor disclosures weaken the cornerstone of good governance and provide scope for insider trading, as important details are available to a chosen few. The data filed by many big corporates reveal a glaring lack of depth.. since the SEBI has compelled the companies to disclose more of the material events, the present researcher does not consider it as significant. The companies are ready to
provide only some skeleton information. They are not willing to share the maximum information, which may be required by the shareholders to assess the situation. Two such disclosures are presented below.

Bland merger: The board of directors of Sundaram Finance has approved a scheme of amalgamation to merge Sundaram Finance Services Ltd., a subsidiary, with the company, after obtaining consent of the shareholders and approval of the Madras High Court. Sundaram Finance Services is a subsidiary of Sundaram Finance, and shareholders can be expected to know the numbers and the background of the company, but such a filing would be more meaningful only if the financial implications for revenues and earnings are indicated (at least for the latest year). By providing the numbers, a better appreciation of the merger and swap ratio may be possible. Otherwise, it is just a bland announcement.

Product plan: Tata Engineering and PSA Peugeot Citroen have agreed to work together to examine the feasibility of jointly developing a car on a PSA Peugeot Citroen platform for manufacture by Tata Engineering for the Indian market as part of its passenger car business. Subject to feasibility, the car may also be considered for overseas markets. This may seem comprehensive prima facie. But the newspaper versions of the move gave so much more information, including the possible target market, the possible timing of the launch, and so on. In such cases, the press release as well as significant comments made by top management on such moves should be made an integral part of the filing. For the latter, even a time lag of a day or two may be allowed as these usually come up in press conferences and follow-up interviews.

Closely-held deals: The board of Kotak Mahindra Finance has approved the proposal for merger of Pannier Trading Company Pvt Ltd. with itself. The merger proposal provides for 25 equity shares of Rs.10 each of KMF for every equity share of Rs.10 each of Pannier. Of all the risks faced by investors in the listed companies, a merger, or any other deal, with an unlisted company is the
biggest. In this case, the lure of the merger was that Pannier owned 75 per cent of Kotak Securities. But very little was known about the overall profile of Pannier and Kotak Securities (in terms of financials). With the swap ratio set at 25 shares of Kotak Mahindra (a well-known listed company) for one share of Pannier, more information should have been forthcoming.\

Therefore, with reference to transparency, one can conclude, that the listed companies in Tamil Nadu are revealing some information though not required by the statutes. However, they can reveal still more information. Regarding the material events, the general trend is that incumbent management is not ready to reveal the entire picture. They are ready to reveal as little as possible, in order to satisfy the listing agreement conditions. But for the conditions in the listing agreement, one would not expect so much revelation.

4.10 INDEPENDENCE OF THE BOARD

One of the prerequisites for the board to perform its roles efficiently and effectively, is to be independent of the management. From a structural point of view, this would mean that the board should be capable of changing the managing director whenever the lower tier fails to delivery the results. If the board is capable of effecting the change in the second-tier management when the management is not performing well, the board is said to be independent. To ascertain the independence of the board in the prevailing situation, the present researcher uses some criteria. The criteria for judging the independence of the board, used by the researcher in the present study, are factors like domination of an individual or group inside a board, submission of the proposals in the board meeting etc., practice of recording the dissent note in the board meeting etc.

In theory, board of directors are elected by a company’s shareholders. In this sense they are accountable to the whole body of shareholders, and not to a

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group or an individual by virtue of their position like promoter. The directors, individually, should be loyal to the shareholders and not the promoters. The Board of Directors is supposed to select the CEO and delegates to CEO the necessary authority to run the show. In turn the CEO chooses his sub-ordinates and creates the second-tier management. Therefore the board is the supreme authority, as far as the management is concerned. Similarly, if the CEO is not delivering the results, it is the moral duty of the board to fire the existing CEO and hire a suitable hand. In short, the board should be independent.

4.10.1 Independence of the Board and Promoters

In practice, however, the promoters has stepped in to the shoes of the board. They run the entire show. It is the promoter who chooses the board members. The promoter recommends the names of the individual directors in the annual general meeting. By virtue of the promoters backing and support only, the individual directors are able to get a berth in the board. Similarly the promoter becomes the CEO or chooses his confidante as the CEO. In most of such companies, only with the approval and blessings of the promoters, even the second-tier management is constituted. Question number 64 was included in the questionnaire to ascertain the fact that whether the CEO is related to the promoter or not. The responses are tabulated in the table given below.

<table>
<thead>
<tr>
<th>Relationship</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Promoter himself the CEO</td>
<td>18</td>
<td>23</td>
</tr>
<tr>
<td>Belongs to the Promoter family</td>
<td>43</td>
<td>55</td>
</tr>
<tr>
<td>Unrelated to promoters</td>
<td>17</td>
<td>22</td>
</tr>
</tbody>
</table>

Source: Primary Data
It is the promoter who becomes the CEO in a number of cases. Table 4.29 reveals that in 23 per cent of the companies surveyed, the promoters have been the CEOs and in 55 per cent of the companies, the promoters' relatives have been the CEOs. There is a statutory limit to the number of companies one can act as managing director. Hence whenever the promoter crosses a limit, they are compelled to select some one else to his liking. Hence 55 per cent of the managing directors are happened to be the relatives of the promoters. It is the promoter who practically enjoys the right of reviewing the performance and taking the necessary remedial action. Many time, the individual directors are thrown away from the board only because of the reason that the individual director may not be having good relation between the promoter. Therefore the hiring and firing right is not enjoyed by the board, as envisaged by the Companies Act. It is only the individual promoter who wields the ultimate authority. The independence of the board is a mockery in the Indian context. Still the corporate sector is in the evolutionary stage in India, compared to the developed countries like U.S.A. Even in the U.S.A., the position is similar to Indian corporate scenario in the early nineties. The only question is the timing i.e., when the board becomes really independent of the promoters. At present, the company is managed by the promoters. Even the abolition of the managing agency system does not help the legislators, what they want to achieve in full. The promoters in the earlier occasion managed the companies through the managing agency system. Now they are able to have a perfect control in the affairs of the company through the Board of Directors.

The facts stated in the preceding paragraph i.e., the board itself is constituted by the promoter is also proved by the responses of the secretaries. A number of particulars related to the directors are solicited from the respondents. One such information is whether the director is related to the promoter group or not. The responses were recorded in table number 4.30.
Table 4.30

Directors related to Promoters

<table>
<thead>
<tr>
<th>Directors related to promoters</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>0-25 per cent</td>
<td>41</td>
<td>52</td>
</tr>
<tr>
<td>25-50 per cent</td>
<td>24</td>
<td>31</td>
</tr>
<tr>
<td>50-75 per cent</td>
<td>7</td>
<td>9</td>
</tr>
<tr>
<td>75 – 100 per cent</td>
<td>6</td>
<td>8</td>
</tr>
</tbody>
</table>

Source: Primary Data

The responses show that in 52 percent of the companies, the board was filled up with individuals up to 25 per cent of the total strength of the board, who have been related to the promoters. In 31 per cent of the companies the promoters’ relatives in the board falls in a range of 25 to 50 per cent. Only in 13 per cent of the companies the strength of the board is numerically dominated i.e., more than 50 per cent of the directors who are the relatives of the promoters.

4.10.2 Proposals for the Board Meeting

The purpose of the board meeting is to make decisions. Decisions are made by passing resolutions. The proposals if accepted by the meeting becomes the resolutions. Proposals are introduced in the meeting and after a thorough deliberation, if accepted by all members of the meeting, the proposal is said to be accepted and it becomes the decision of the meeting. Once it is accepted by the meeting, it becomes a resolution. To file the proposals, it requires careful study of the business environment as well as thorough understanding of the internal constraints. Therefore one can come to a conclusion regarding the contribution towards the functioning of the board on the basis of the proposals submitted by the board. To assess the contribution of the individual director, information is
solicited from the respondents regarding the proposals filed by executive directors and non-executive directors. The relevant questions are reproduced herein below:

"38. Average number of proposals introduced by the non-executive directors during the last 5 years.
39. Average Number of proposals introduced by the executive directors during the last 5 years".

The responses to the above questions are tabulated in tables 4.31 and 4.32

<table>
<thead>
<tr>
<th>Table 4.31</th>
<th>Proposals by Non-Executive Directors</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Proposals filed by non-executive directors</td>
</tr>
<tr>
<td>Yes</td>
<td>18</td>
</tr>
<tr>
<td>No</td>
<td>60</td>
</tr>
</tbody>
</table>

Source: Primary Data

<table>
<thead>
<tr>
<th>Table 4.32</th>
<th>Proposals by Executive Directors</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Proposals filed by Executive Directors</td>
</tr>
<tr>
<td>Yes</td>
<td>10</td>
</tr>
<tr>
<td>No</td>
<td>68</td>
</tr>
</tbody>
</table>

Source: Primary Data

The responses of the secretaries revealed that only 23 per cent of the companies had received some proposals from non-executive directors. This indicates the involvement of the directors in the company. 77 per cent of the companies have categorically declared that non-executive directors had not submitted any proposals. Even in the companies where the non-executive directors had submitted the proposals, the number is very meagre. Out of 18 companies in which the non-executive directors had filed proposals, the total number of proposals received during the last five years is only one in one company. The maximum number of proposals received among that group in one company is only five during the last five years period. Had the non-executive directors been active and more involved, more number of proposals would have been introduced by such directors. Only in 10 companies i.e., 13 per cent of the companies the executive directors have filed the proposals, a meagre number,
compared to non-executive directors also still more worse. The responses to the above two questions indicate that the directors lack involvement. Therefore in general, we can conclude that the decision making authority is only with the promoter group. Hence no independence for the board. As the majority of the directors are not involved in the submission of the proposals, it seems that the promoters’ group alone submit proposals. The directors are not getting involved in the affairs of the business. They are maintaining distance from the business. They leave everything to the promoters’ group. Hence, they lack independence.

The purpose of the board is to make decisions in order to manage the company. Decisions are made by introducing a proposal, deliberate it in the meeting. After thoroughly deliberated the issue, the decisions have to be taken. Therefore, the proposal is the base of the decision. The independence of the board can also be judged from this angle. Therefore a question is included in the questionnaire, to judge the independence of the board. The relevant question is:

“29. Normally who introduces a proposal in the Board Meeting?
   i) Chairman     ii) CEO       iii) Executive Director
   iv) Non-Executive Director v) Nominee Director”.

**Table 4.33**
Submission of Proposals in the Board Meeting

<table>
<thead>
<tr>
<th>Proposals submitted by</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chairman</td>
<td>65</td>
<td>83</td>
</tr>
<tr>
<td>CEO</td>
<td>13</td>
<td>17</td>
</tr>
<tr>
<td>Executive director</td>
<td>Nil</td>
<td>-</td>
</tr>
<tr>
<td>Non-executive director</td>
<td>Nil</td>
<td>-</td>
</tr>
<tr>
<td>Nominee director</td>
<td>Nil</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: Primary Data
The responses to the above query clearly show that under most of the circumstances, the proposals have been filed by the Chairman only. In 83 per cent of the companies, it is the chairman who has brought a proposal and only in 17 per cent of the companies, the CEOs have brought the proposals. The responses corroborate the conclusion arrived at with reference to responses discussed in table number 4.30. From the above responses it is clear that the Chairman or CEO alone are bringing the proposals. Simply the board members are endorsing the proposal and pass it as a resolution. This shows that the entire board is not deciding in what to and what not to do. The silent endorsement does not speak well about the proper functioning of the board. One more evidence, in favour of lack of involvement. Simply they are attending the meeting whenever it suits them and convenient to attend. Another fact to prove that the board is a constitutional board i.e., the board is there to satisfy the legal requirement.

The independence of the board is also tested from another angle, i.e., the decision making authority. The relevant question bears the number 20. The relevant is given below.

"20. In the event of decision already taken outside the Board Meeting and subsequently got ratified in the Board Meeting, who is the real decision-maker?
   i) Managing Director ii) Chairman iii) Outsiders"

The responses to the above question revealed that in 51 per cent of the companies the chairman is the decision maker. Managing director is the decision maker in 30 per cent of the companies. One related question to the above question is included in the questionnaire with the number 20a. The question is given below.

"20. a) If, Outsider, the individual who takes the decision is:
   a. Member of the Promoter family
   b. Not related the Promoter family
   c. Representative of the holding company. “

The response to the above question is surprising. In 90 per cent of the companies, the decision is taken only by a member of the promoter family.
4.10.3 Remuneration to Non-Executive Directors

Usually the non-executive directors are entitled for the sitting fees and travelling allowance for attending the board meeting. One cannot expect an individual to devote his time and energy just for a sitting fee of Rs.1500 or Rs.2,000. In a situation, where the company is stand to gain in crores of rupees but the individual directors are not benefited, it is natural that no non-executive directors are very much interested in the activities of the company. The researcher is shocked to ascertain the fact that only one company out of thirty companies in the Sensex list, rewards the non-executive directors with one per cent of net profit as remuneration. The directors in the remaining companies are eligible only for sitting fees and travelling allowance. Under the circumstances, no body expects positive contribution from the individual directors for a non-remunerative job. Again it is clear, that the directors are not getting involved in the affairs of the companies. Moreover one cannot expect men with business acumen and expertise to contribute their expertise free of cost. Morally, the companies cannot bind the directors to contribute the cause of the companies.

Similarly, to test to the extent to which the non-executive directors are remunerated in the companies selected for the study, the following questions were asked:

"18. Are the non-executive directors entitled to any other monetary benefits other than Sitting fees and TA: Yes  No"

<table>
<thead>
<tr>
<th>Eligible for benefits</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>No</td>
<td>69</td>
<td>88</td>
</tr>
<tr>
<td>Yes</td>
<td>9</td>
<td>12</td>
</tr>
</tbody>
</table>

Source: Primary Data
In 88 per cent of the companies the non-executive directors have not been entitled for any benefits, other than travelling allowance and sitting fees for attending the board meeting. Moreover, the responses to question number 17, the secretaries responded that the sitting fees have been paid, as per the provisions of the Companies Act, 1956 only and actual travelling expenses will be reimbursed. Hence from the angle of monetary benefits, the boards of the majority of the companies are not benefited. Therefore one cannot expect the business tycoons and experts to devote their time and money to the cause of a company without any reciprocal benefit. Therefore, the system should be modified in such a manner, that the non-executive directors should be entitled to get remuneration in all the companies and that should also be linked to the profits. However, the directors can be said to be independent as they are not in receipt of any remuneration.

"Q.18. (a) If Yes, please state the nature of payments"

Only twelve per cent of the companies have given extra remuneration for directors. Such directors are getting remuneration in the form of co commission at one per cent of net profits. The responses to the questions 18 and 18a once again proves that the directors lack commitment and involvement. Their continuance in the board is a gift to them by the promoters. Hence, the directorship depends upon the patronage of the promoters' group. Hence the directors are not independent.

4.10.4 Domination in the Board Meeting

The manner in which the board meeting was conducted clearly indicates whether the board is independent or not. An item is included in the questionnaire to the independence. The relevant question bears number 25.

"25. Do you sense the domination of a single individual in the conduct of the Board Meeting? Yes No"
Table 4.35  
Individual Domination in the Board Meeting

<table>
<thead>
<tr>
<th>Domination</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>60</td>
<td>76.9</td>
</tr>
<tr>
<td>No</td>
<td>38.18</td>
<td>23.1</td>
</tr>
</tbody>
</table>

Source: Primary Data

The responses of the secretaries give a signal to infer whether the board is independent or not. Around 23 per cent of the companies have categorically stated that they are not sensing the domination of any single individual compared to 77 where the domination of an individual is noticeable. Hence numerically, the responses suggest that the board is not independent.

Another instrument to judge the effectiveness is the participation of the members in the meeting. Table 4.22 and 4.23 indicates that both executive directors as well as non-executive directors are actively participating in the meeting. From this angle, one can be satisfied that the boards of listed companies in Tamil Nadu are performing well.

4.10.5 Practice of Recording Dissent Note

The purpose of the board is to evaluate the performance of the management. Therefore the board meeting should not be merely a ritual of assembling, signing the registers and disbursing. One of the functions of the board is to review the performance of the second-tier management. This exercise is a must to take the company to the desired destiny. The deliberation process is an important technique through which the board purpose will be achieved. Deliberation process leads to either unanimity of decisions or at times the members of the board may be at loggerhead. Unanimity cannot always be arrived at or aimed. Differences of opinions are bound to arise.
effectiveness of the functioning of the board can be judged by observing how the
seriously the process of deliberation is carried out. If the members are really
independent, they may not hesitate to state their objection or take a stand against
the proposed decision. Further, the members may even try to record their
objection. Such recorded objection will save them in future, in the event of any
probe. However, such objection will come only if the directors are independent.
If they are diffident and if they do not want to create an embarrassing situation,
they may keep silent, even if the activity is objectionable. Therefore, one can
evaluate the independence of the board by observing the deliberation process
from this angle. To ascertain whether the board is independent or not the
following question has been included in the questionnaire.

"Q 22. Does Director insist on recording his dissent, if made, in the minutes of the Board
Meeting?"

The responses to the above question have been tabulated in Table 4.36

<table>
<thead>
<tr>
<th>Directors' Dissent Note in Board Meeting</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Insist on recording dissent</td>
<td>12</td>
<td>15.38</td>
</tr>
<tr>
<td>Does not insist on recording dissent</td>
<td>66</td>
<td>84.62</td>
</tr>
</tbody>
</table>

Source: Primary Data

The responses revealed that in a majority of the companies and that too
around 85 of the companies’ board witnessed unanimous decisions. The
response of the company secretaries in many cases is ‘unanimous’. Really, it is
disturbing to note that all the decisions of the board are always made by
consensus without any dissent. Some companies also observed that no such
circumstances ever prevailed. Either all the decisions are made to the fullest
satisfaction of all the board members or out of compulsions such unanimous
decisions might have been made. Such occurrences (always unanimous
decisions) are doubtful. The researcher attributes such unanimous decisions, in most of the companies under all circumstances, as a result of lack of independence of the directors. To confirm this pattern, yet another question is asked. The relevant question is:

"Q.23. If so, during the last 5 years, how many resolutions had been passed with the dissent note?"

In the last 5 years, totally, 14 resolutions had been passed with the dissent note for all the respondent companies (78). Again, this volume is positively pointing towards lack of involvement and independence of directors. As pointed out earlier, that giving berth to a person in the board room is a favour extended to an individual enabling him to enjoy a number of concessions. Though the directors are supposed to have represented the shareholders in general, their loyalty is only towards the group which is in control of the management.

True independence comes when the directors are individually informed about the company’s affairs and make their decisions keeping the long-term interest of the company in mind. The researcher attempted to evaluate the independence of the directors, from this angle. Hence the following question was included in the questionnaire:

"Q.26. In the absence of the Board Meeting, is there any practice of informing the Directors about the performance of the company?
Yes No"

Table 4.37

<table>
<thead>
<tr>
<th>Practice of sending information</th>
<th>Number of companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not Applicable</td>
<td>17</td>
<td>22</td>
</tr>
<tr>
<td>Yes</td>
<td>43</td>
<td>55</td>
</tr>
<tr>
<td>No</td>
<td>18</td>
<td>23</td>
</tr>
</tbody>
</table>

Source: Primary Data

The responses to the question number 26 was given in table number 4.37 which revealed that 22 per cent of the management is not at all giving the scope to the individual directors for demanding the information as they are regularly
conducting the meeting. Hence no such occasion. Only 23 per cent of the companies have expressed that they are not informing the individual directors. The balance, 55 per cent, of the companies were taking the steps to convey the information to the directors. One more related question to the above one is included in the questionnaire, bearing number 27. The relevant question is:

27. If so, the nature of information provided to Directors under such circumstances:
   i) Account
   iii) Statement about sales
   v) Labour relations
   vii) Any other (Please specify)

The secretaries of the companies revealed that in 23 per cent of the companies, the directors will demand the information. Of the directors demanding the information, 60 per cent of the directors will demand information pertaining to accounts.

The conclusion that can be drawn from the responses to the above question is that a majority of the companies are providing the necessary input to individual directors to evaluate the performance of the company. The above discussion may lead one to conclude that the board is independent. The discussions elaborated in 4.10 clearly converge to a single point viz., that the boards of the companies in Tamil Nadu are not independent. One more question on the similar line included in the questionnaire is question number 16. The responses of the secretaries for the above question revealed there is no for demanding additional information, as the necessary information is always supplied with.

4.10.6 Process of Re-election

If the legislators are seriously interested in installing an independent board, the board election process should be streamlined, apart from other things. More should be done to provide information to the shareholders on the performance of the individual director wishing to be re-elected. The researcher
has gone through several annual reports to find out how the companies in India are presenting the information regarding the directors who are seeking re-election. The information content for new director is also gathered. Not only companies in Tamil Nadu, but also companies listed in a number of other stock exchanges are taken for the study. To the shock and surprise of the researcher, the information provided with reference to the retiring director who is seeking re-election, was very short and crisp. Since the act classified such business – election of directors - as ordinary business, there is no compulsion to give any details of the candidates who is contesting. As a matter of passing reference, the board usually thank and congratulate such directors for their valuable services. Annual reports do not reveal anything about the director's contribution. Moreover, it is rather rare to witness a situation where the retiring directors are not seeking re-election. If there is any dispute between the incumbent management and the concerned individual director or the groups to which such individual director belongs to, such director may not opt for re-election or may be dropped by the controlling group. Death is another factor which may create such a situation. Therefore performance is not the criterion for proposing a candidate for the position of directors. Relationship with the incumbent management is the influencing variable for getting a berth in the board. A question is asked to the respondents about the directors who had not been re-appointed. Such cases seem to be rare.

"Q.62. In the last five years, any director who retired by rotation had not been re-appointed?"

In the last five years only in 11 companies the directors who retired had not been re-appointed. Around 86 per cent of the companies have stated that none of the retired directors had not been re-appointed. It shows a stagnant board. The adage that nothing is permanent except change is not applicable to Indian boards. Again, the reason for being getting an accommodation in the board is only a favour extended to the concerned individual. Another related question is included in the questionnaire and the question is:
Of the eleven companies which stated that the retiring directors had not been re-appointed, seven companies had expressed the reason for such non-extension is death and in the remaining cases, the secretaries had mentioned the reasons as other 'reasons'. Therefore, it is clear that the performance of the directors is not the criteria for the extension or re-appointment. Death alone can prevent the re-appointment and not performance.

In India, the companies have to file a statement with Registrar of Companies some brief information like age, number of directorship in other companies, address etc. Even such information is not provided to the shareholders through the annual report. The career history of the directorial candidate should be disclosed to shareholders in the Annual Report. Companies sometimes fail to disclose, intentionally or unintentionally, the past career history of the candidates seeking either election or re-election to directorship. These are important to shareholders to judge the suitability of the candidate, especially if the candidate has been associated with a past corporate failure. Shareholders need full disclosure, if they are to judge whether a non-executive director is independent. Shareholders require full 'warts and all' disclosure, for non-executive director, a full record of his or her part as well as current carrier which is necessary for an assessment of independence.

At the least, shareholders should be made aware of any professional, political or family relationships that exist between the candidates who is contesting for the director position. The researcher doubts why the information need not be provided to the shareholders who should know all these details. It is interesting no note that the Birla Committee stipulated that the company should give the following details who are seeking either election or re-election:
The Committee recommends that in case of the appointment of a new director or re-appointment of a director the shareholders must be provided with the following information:

- A brief resume of the director;
- Nature of his expertise in specific functional areas; and
- Names of companies in which the person also holds the directorship and the membership of Committees of the board.

It will be interesting as well as thought provoking to study the position prevailing in other countries especially in developed countries like U.S.A., and U.K. The Listing Rules for the London Stock Exchange require annual reports to contain a "short biographical note" for non-executive directors only, but the rules do not specify what such a note should contain. Therefore the companies listed in London Stock Exchanges provide a short biographical note for the directorial candidates. Disclosure of directors' biographical details is erratic. PIRC, an active corporate governance activist in U.K., accusing that companies are providing superficial career histories of directors seeking re-election or standing for the first time.39 "Short biographical note" is not a must as per the rules of either the Companies Act, or the listing agreement.

The practice of U.S.A., is still more better compared to U.K. practices. According to the rules of the listing agreement in U.S.A., the names of the directors who fail to attend 75 per cent of the board meetings are to be named in the annual reports. The record of all the companies, in India including the companies which have been rated as the number one in terms of disclosure, is very poor in this regard. One of the reasons for the ineffective functioning of the board is the institution of Non-Executive Directors. The legal theory recognises the Board as the top most organ of the management charged with the responsibility of governing the enterprise and board delegating its authority to the CEO. Yet in actual practice, the Board of Directors is an institution created

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39 Ibid
by the promoter. Hence, the Board of Directors has become a legal fiction. The board is constituted because of legal compulsion.

The Indian boards have not yet graduated to the professional board level, where the board really delegates the authority to CEO. However, in developed countries like U.S.A., and U.K., the board really delegates the authority to the CEO. If the board finds that the CEO is not performing, he will be thrown away. Under such circumstances, with the passage of time, the chief executives, being whole-time officers of the company, can naturally devote greater time and attention to the matters connected with the management of a company. It is very easy for individuals who are busy otherwise in their own vocations and are serving as part-time directors on a board to defer to the expertise of the management and believe everything they hear. Again the attribute of independence is lacking from the board. The director serves the company best only when he or she makes independent inquiries, and is not afraid of asking uncomfortable questions that may even embarrass the Chairman or CEO in the pursuit of what is best for the company. An effective board is one which is neither made up of owners nor employees. The directors can be labelled as independent only if they are willing and able to assert themselves on the functions of review and strategy formulation.\(^{40}\)

Independence of the individual directors are circumscribed by a number of factors such as their allegiance, loyalty or friendship to the managing group, lack of relevant information, and even lack of adequate time to devote to the affairs of the company. Another reason attributable to the independence of the board, the remuneration package available to the non-executive directors is very poor.

\(^{40}\) Ralph D. "Corporate Accountability, 10 Things you know about corporate Boards that are wrong". Address by Publisher, Boardroom, Insider, newsletter and author, Delivered to the Economic Club of Detroit, Detroit Michigan, March 2, 1998
4.11 ATTITUDE OF THE SECRETARIES TOWARDS THE BOARD

To ascertain the view of the secretaries who are on the scene and closely watching what is happening inside the board, are in a better position to express whether the board is independent or not. Hence the present researcher has decided to study what the secretaries feel about the independence of the board. The researcher for that purpose has used the following statements to study the attitude of the companies secretaries towards the boards' independence. The following statements are prepared to measure the attitude of the companies' towards the board independence. All the statements are constructed only from the angle of independence. Hence, the consolidated score is taken for the interpretation of the survey results. The statements constructed for the measuring the attitude of the secretaries towards the independence of the board members are given below.

"Q.75. The board meeting is only a ritual where it is considered as a get together. S.A. A NI DA SDA "
"Q. 76. The directors freely and actively participate in the proceedings of the board meeting. S.A. A NI DA SDA "
"Q.77. The individual directors are dominated by the members of the incumbent management in the board meeting. S.A. A NI DA SDA "
"Q.78. The directors are acting independently in the board meeting. S.A. A NI DA SDA "

The analysis of the responses for the above statements revealed that the total score for all the respondents amounted to 468. The average score works out to 6, as compared to the maximum possible score of 20. Therefore the percentage of agreement to the attribute of independence is only 30 per cent. The above statements are framed only for evaluating the attribute of independence of the directors. Hence, the interpretation of the total score alone is attempted, as they are supposed to reveal only one attribute. The statements are not individually analysed.
Hence, from the responses of the secretaries towards the independence of
the board and other information collected, the present researcher concludes that
the board is not independent.

4.12 CURRENT SCENARIO

Barring a few companies in India, the board is nothing more than a
statutory imposition. However, not much of resistance is used to be raised. That
is the order of the day. Directorships of companies is looked upon as something
like a favour extended to the individuals. Nine out of ten times when a decision
is taken which is not in the best interest of the company the people at the level of
the board are fully aware of what they are doing. Professionals also know that
correct decisions are not taken as would be expected of agents and trustees but
they endorse it either out of compulsion of family arrangements or take it in the
best interest of the promoters and make themselves to believe that what is good
for promoters and management is good for the company. Some times they
even do not bother about law.

An incident of late 70's could be cited to highlight how professional
directors who are supposed to be independent behaved. When giving
advertisements in souvenirs brought out by the political parties was bad in law
even according to the circular issued by the Company Law Board and a legal
opinion obtained by FICCI from an eminent Jurist and circulated to its members
and yet companies, one after another went on giving advertisement in the
souvenir brought out by the ruling party. The best of professional directors,
eminent counsels, retired judges, including Chief Justice of Supreme Court of
India who sat on the boards of these companies voted for giving these souvenir
advertisements. The problem with the members of the board is best described by
the attitude of Duryodhana in Mahabharata when he says that “I know what is
right but I am not able to act accordingly and know what is wrong but I am
unable to restrain myself from doing it. People are invited to sit on boards because of their names. Going by the sheer number, it is doubtful that they would be able to make any meaningful contribution to the growth and progress of any of these companies. Getting on the board depends generally on how well he knows the company or the family that owns the business. Board appointments do some what reflect the old school-tie net work or golfing buddies. Company boards are packed with relatives and friends who are mere nodders at the meetings. Some directors who have been accommodated in the board as eminent persons in their profession as lawyers and auditors, used to quote that they have never seen any officials or the company premises. Usually board meetings are conducted in five star hotels or in some picnic spots.

The standard of corporate governance has been poor in India because of historical reasons. The world over, corporate governance has grown from family managed companies to the professionally managed ones. But in India, corporate management is still in the early stage of family-managed companies. Such companies do not attach much importance to corporate governance, as they consider the entity as an extension of a proprietary outfit. As a result, most of the important investment and operational decisions are not taken as the agent of the shareholders of the company. On the other side, the promoters know well, that their money is not at stake. Hence, they spend it in a lavish manner without any commercial prudence and judgement. Siphoning off funds, to the concern which is wholly owned by the promoter, is the normal course of action. Neither the shareholders, both individual as well as institutional, nor the board members check such practices which lead many companies in India to bankruptcy. The suicidal nature of the activity – for the company - is not at all realised by the board of the directors. This practice prevents from living like a river company.

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41 D.S.Mehta, "Corporate Governance: Role of Professionals", Chartered Secretary, May 1997.
as mentioned in the first chapter. The promoters knowing well the consequences of such diversion of funds are going on merrily without any check.⁴²

According to the Goswami Draft Report, while the key to good corporate governance is a well functioning board of directors with a core of independent and acclaimed non-executive directors, the board of most Indian public companies fail to make the mark in this respect. The report states that it is incredible that a country with such a large talent pool of professionals does not have a larger pool of committed non-executive directors. The fact that such a pool has not come into play in the corporate world is because Indian companies do not search for such people and choose the comfortable risk-less options of selecting non-executive directors from a small coterie.⁴³

A study of the boards of the top 100 listed private companies reveals that most of them are numerically dominated by executive directors or are packed with required corporate executives, bureaucrats, family members and well-wishers who wish to have no say in the companies, or by executives of other group companies.⁴⁴ A typical Indian board.

In general, boards are reluctant to question the decision of the management, even when they have reservations. What at best they can accomplish is, cleaning up after the event. The boards should, therefore, demand a reasonable performance from the managing director, say over a period of three-to-five years timeframe. If the managing director falls short of a set of standards, the board should find a successor. In no case, succession planning must be the preserve of the outgoing CEO. As for transgressing the bounds of law, the enforcement agencies should have a pro-active role, not just reactive in dealing with illegalities. Top management should make it a point that it will not take kindly to infractions of the law. If the CEO is receiving kickbacks or

⁴³ Ibid
⁴⁴ Ibid
siphoning off funds, in ways affecting the overall corporate performance, then it lies well within the bounds of the board and only its vigilance can help matters.

The issue, in India particularly, is not only what law requires, but what the Board should actually focus on. Law requires the Board to decide on borrowing, lending or investment of funds, adoption of report and accounts and recommending dividend. While these are important, are they the limits of involvement? Quite clearly, they are not. In successful companies, the Boards discuss annual operating plans, capital budgets, monitor results against pre-set targets, review competition and economic and political events – and accordingly steer the business processes and infrastructure. Their focus should at all times be on service to the customer and the consumer, thus creating shareholder value.⁴⁵

However, if one goes through the journals and periodicals, the spines are getting started chilling. Promoters belonging to the old generation as well as new promoters have started failing the gullible investors. As a result captains of the industries, both belonging to the old generation as well as new generation are getting worried about the behaviour of the their brethren. To site a few example, how they are agitated, the researcher is presenting the reported speeches and texts of the captains of industries in India.

"However, often, one come across examples of corporate behaviour that is not in tune with this expectation. Consider the following:

In 1985, a family-owned public corporation located in Northern India, in which the family owned 9 per cent of the equity, refused to register a 14 per cent stake bought by a Non-Resident Indian (NRI). They even had the backing of the government of the day, which had changed the law to say that no more than 5 per cent of the shares could be held by an NRI.

⁴⁵ K.B. Dadiseth, Chairman, Hindustan Lever Ltd., "Corporate Governance In India", 32nd A.D. Shroff Memorial Lecture delivered under the auspices of the Forum of Free Enterprise.
A highly respected multinational corporation situated in Eastern India has allegedly fixed its books to show high exports, high profits, etc. But, of course, this is on subsidy.

As many as 2500 of the 3900 companies that got listed between 1991 and 1996 have completely disappeared. It is almost impossible to discover what happened to these corporations as there are no annual reports or any other form of published information about them.

A well-known company in Western India wrested control of a prestigious multinational construction company and removed the Managing Director against the wishes of a majority of the other shareholder.

This incident in Bhopal is an excellent example of how a company, not willingly of course, but because of lack of due diligence in its systems, did not discharge its obligations to society in general.

There is a clear pattern that one can discern in all this. An individual or a group of individuals in these corporations have taken decisions that benefit only a small select group, to the detriment of the large body of shareholders. This is against what is universally known as the Principles of corporate governance. The first reason is the feudal mind-set that exists in India. Unfortunately, in this country, thanks to this feudal mind-set that has existed from times immemorial, the progeny has controlled the throne. From the days of the proverbial monarch throne, we have come to the days of corporate throne. There is a tacit assumption that the son or the daughter of an owner has the birthright to assume positions such as Director of the company as well as Chairman and Managing Director. The competence of the scion in question to manage these high positions, is a less important criterion for the appointment for that position. The above comments are from the most admired CEO of a company which is a trend setter for good corporate governance.
“Family must be restricted to boards, rather than management. But admitting you are not competent isn’t easy” Bajaj Auto CEO Rahul Bajaj, says on the way Indian business families need to reinvent themselves. The above statement is a testimonial to the fact that the core group which controls the corporate kingdom is not duly qualified. It also shows that the family members interfere in the management. Now the question is, is it right on the part of the promoters even to fill the board. Filling up the board by their friends and relatives have landed the Indian corporate sector to such a miserable situation. Not only the companies are in trouble, it affects the entire society. As observed in the earlier paragraphs, the corporate sector is the engine of growth. Therefore, the performance of the corporate sector reflects in the economic development of a country.

Scam after scams are the results of such bad corporate practices. Witnessing the messy corporate affairs, new generation entrepreneurs take the wrong clue from the prevailing corporate practices. That is why 2500 companies are in the wanted list out of 3900 companies which have tapped the capital market during 1991-1996. Out of the remaining 1400 companies, actively traded scrips are countable. Most of the shares are traded below the par value – available at around 10 to 20 per cent of the face value. Why is this miserable situation? The reason being the new generation entrepreneurs have tried to imitate the existing genre.

The corporate citizens have demonstrated how well they can behave. One thing is certain. All the corporate citizens have proved that their respect for the law is indifferent. This is true for all the corporate citizens, whether the nature of company, either professionally managed companies, multi-national companies or companies promoted and managed by Indian entrepreneurs. Exploitation of opportunities is considered as a business. The nature of the company never

prevents the management in practising in unethical or illegal ways. To the maximum possible extent, the persons the power want to exploit the situation. The following lists prove the above mentioned facts. The bad precedents are set by both companies managed by professional managers as well as promoters managed companies. The unethical practices are noticeable both in Indian companies as well as Multi-National Companies. Promoters of established groups as well as new born promoters are equally competitive in practising unethical, unfair and illegal practices. Some of the practises adopted by the corporate community are given below along with the name of the practitioners:

(i) Peerless General Finance & Investments Ltd. – Lack of transparency.
(ii) CRB Corporation Ltd. – Total financial failure.
(iii) Escorts Ltd. – Chairman and Vice Chairman awarding compensation package to themselves.
(iv) Shaw Wallace – Poor financial management.
(v) ITC Ltd. – Non-detection of excise evasion and FERA violations.
(vi) Apollo Tyres – Family rift over control.
(vii) J.K. Synthetics – Infighting between two brother directors leading to stagnancy of business operations.
(viii) Modi group – Financial Institutions coming to intervene in family disputes.
(ix) L & T – Take-over threat by Reliance group.
(x) M.S. Shoes – An attempt to cheat the investors.\(^\text{48}\)

In some cases their mental attitude as the monarch of their corporate kingdom is revealed, which is unjustifiable. Eicher or Reliance Industries, which is today considered highly professional, there’s little that a professional manager can do to reverse the decisions of owners even now. Even in the house of Tata, with Ratan Tata tightening his grip over the group, did the satraps of the JRD era even have a chance? The answer is, well, history. The former CEOs of TATA enterprises like TISCO, Tata Chemicals, who were all appointed by late

J.R.D.Tata. They were subsequently dismissed by Ratan Tata, the successor of late J.R.D.Tata. The only reason for their dismissal was that they are not subservient to Ratan Tata. This list is a long one. Russi Mody and Darbari Seth, Nani Palkhivala, Ajit Kerkar were some of the yester-year heroes of TATA group companies but sent out of the group as they refused to accept Ratan Tata’s views. If this is the attitude of the captain of one of the India’s largest conglomerate, one need not wonder how other bosses in India behave. It is the mental attitude of Ratan Tata to behave like this ignoring the performances of the managers of repute. If Ratan Tata challenges them on the grounds of performance, then he would have relinquished his position as The Chairman of a number of Tata Companies which are not performing up to the expected level.

In India now the promoters have started realising the advantages and the need to have an independent board. They have started re-aligning the board. There is a gradual shift from the family members packed board to independent board. This an evolutionary process. It may be the result of the exigencies.

One such revolutionary change witnessed in the post-LPG era was the constitution of supervisory board. The largest shareholders of Eicher Group’s holding Company, Vikram Lal – who holds around 70 per cent in Eicher Goodearth - stepped down as Chairman and the corporate circle was excited to witness a new phenomenon so far not accustomed to, which many management gurus have been preaching for a pretty long time. The Chairmanship was handed over to Subodh Bhargava, a thoroughbred professional. The presses and academicians raised a toast to the changing culture of the Indian companies. Though the intention of Vikram Lal is not hand over the management to Subodh Bhargava, the change is for good. In the words of Vikram Lal “I am not giving up control. I was a bit at sea on how to deal with the finer aspects of the group’s governance. If the chief executive is chairman, then who’s to question the chief

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executive? By putting in place a supervisory board, I have actually tightened control.” Vikram Lal had constituted a supervisory board, consisting of five members, including Lal - people with a wealth of experience and high levels of competence, who are considered above board in the industry. Two such members – ex-Lever chairman SM Datta and SCICI vice-chairman and managing director, NC Singhal – have already joined the board. According to Lal “We (the supervisory board members) are not leaders or managers. We are not here to look at operations and strategy. We will review the decisions and the strategies for formulated by the management board (headed by Bhargava). We now have a structure where we’ll have a more formal reporting and review”.

If the trend created by Lal of Eicher Group, appears at the one end of the spectrum, at the other end lies Modi Group. BK Modi, now chairman and managing director of the holding company Modi Corp, has forged joint ventures with foreign partners and has moved away from the day-to-day affairs of his joint ventures. Modi freely admits that he’s learnt all about the xerox business from the Xerox Corporation. Further he says: ‘In a group, every company has to be focussed. I have handed over operations to professionals, even to foreigners where it was necessary. My function is to bring leadership to the business. We today need business leaders.” As head of the ModiCorp, Modi is involved with long term strategy and managing the joint ventures.

Brother Shashi and Ravi Ruia of the Essar group may have been making noises about bowing out of day-to-day operations. They may have hired any number of well-oiled and respected professionals, but the next generation – Prashant and Anshuman is firmly entrenched. “There is nothing wrong with owner-run companies. Usually first generation entrepreneurs build companies. Management gets weak only in the second or third generation,” says Francis

49 “Ratan opens gambit for easing Kerkar out of IHC”, Economic Times, 27.8.97.
51 Ibid.
Pike, director, Peregrine Investments. Yet, across large swathes of Corporate India, second, third and fourth generations are being groomed to take over. says Nikhil Nanda, 23, heir to the Escorts group, now looking after the motorcycles division: “Most family-run organisations manage operations professionally. As company structures are complex, it is not easy for family members to enter into management out of the blue. The ones who finally enter the groomed to take charge.” Majority of the Indian companies’ board are of the above type only.

But severe competition from all quarters, especially from multinational companies, is forcing Indian corporates to bank more on professionals. Says Niraj Bajaj, managing director, Mukand Ltd: “Companies that wait ten years to bring in professionals to head operations may not survive that long. The change is bound to come; it may happen tomorrow”. At Bajaj Auto Ltd., chairman Rahul Bajaj is believed to be grooming a successor. Adds Niraj Bajaj: “The successor has not been decided as yet; it will be done at the appropriate time, and strictly on merit. Just because you are born a Bajaj doesn’t mean you are the best manager around.” At the Bajaj group, management by professional CEOs is top-of-mind. This is more or less in line with international practices – it’s a two-tier management structure that’s in vogue. Non-executive directors from a board that plays a supervisory role and the management board is the one involved in decision-making and strategy. And quite like the management boards in India, US boards have outsiders as directors – FI nominees, for instance. Such outsiders have little time to spare. As a result, Lal has modelled his supervisory board along the lines of German public limited companies, while Modi has modelled his group structure on the lines of Xerox Corporation.

Lal’s moves, or even Modi’s are surely a harbinger of things to come. The demands of business and cut-throat competition may gradually usher in the change. The advantages of letting professionals call the strategies are far too many. More important, it’s imperative in the Indian context. Says Maitreya Doshi, managing director, Premier Automobiles Ltd: “When there is more than
one promoter, their priorities may differ. A professional CEO can always strike a balance.” If a family feuds and bickerings make up for the better part of business stories in India, a professional management acts as a buffer. Says Subodh Bhargava, now chairman Eicher group: “When a family member is running the business, the management tends to become very individual focussed, and when succession takes place, it affects the company. But collective leadership (supervisory board) is less individualistic and so would be a professional CEO.” Bhargava says that Vikram Lal’s son Siddhartha Lal, 26, may enter Eicher if he chooses to, but as assistant manager. The rider: he may get promotions faster, if he performs.

At Asian Paints, the realisation that collective leadership at the top is better and desirable dawned only recently. After ICI Pic acquired a 9 per cent stake in the company, buying out the stake of AP’s most high profile promoter Atul Choksey, the other promoters have quickly closed ranks. Explains Ashwin Dani, single largest share holder of Asian Paints: “We have a perfect blend of entrepreneurial and professional management. If a manager has a bright idea, he has the full independence and support to develop it: he becomes the owners of the management process.”

Intrinsically linked to the policy of laissez-faire is the stake that promoters hold in their companies. Says Lal: “The biggest deterrent for Indian managements to give up management control in favour of professionals is the small size of their holdings. It is insecurity that prevents them from moving out.” Ratan Tata has been often accused of this. As he holds less than 2 per cent in Tata Sons, his detractors say that the Tata satraps were becoming a threat. Perhaps that insecurity might have forced him to send the Tata Satraps like Russy Modi, Dadiseth, Nani Palkiwala and Ajit Kerkar out. In promoter-run companies, decisions may often be taken keeping the owner’s interest in mind, and not the corporate interest, says Shitin Desai, Vice-chairman, DSP-Merrill
Lynch: “Just because promoters do not want to dilute their stake, they keep projects highly geared. This is not acting in the corporate interest.

For Corporate India, it’s a sully long haul before promoters actually give more independence to professionals. The development of insurance companies pension funds, and mutual funds investing in equity is necessary before much can happen. Eicher’s Lal has made a beginning, but is very much in control. The change is not an isolated event. Subsequent happenings in the corporate circle confirms that things are started taking different steps.

Another incident in the corporate India has happened in one of the retail chain group, Biyanis of the Pantaloon group. Yet another family-owned company is restructuring its organisation in an attempt to professionalise management. It is now the turn of the Biyanis of the Pantaloon group to divorce ownership from management. The Biyanis have recently constituted a six-member group supervisory body comprising only of family members, which marks the beginning of its transformation to a non-executive governing body. From now on, the panel will choose chief executive officers from within or outside the family, who will be solely responsible for running the show. While Kishore Biyani has been retained as the CEO of the group flagship Pantaloon Retail (India) for another two years, other family members have been kept out of top level positions.

The group is in the process of appointing professionals to head key business units such as manufacturing & supply chain. The eldest member of the family, Gopal Biyani will head the governing body. Kishore Biyani, Anil Biyani, Rakesh Biyani, Sunil Biyani and Vijay Biyani will be members. Rakesh Biyani, Anil Biyani and Sunil Biyani will continue to be associated with the group companies in various other capacities. The group has also addressed the question of functional overlapping since the companies already have statutory boards. While statutory powers will remain with the board, the governing council will play more of a visionary role. In case of a dispute, CEOs will
resolve it. CEOs will report to both the boards, Kishore Biyani said. The supervisory board has also been given the task of approving the annual business plan of companies and finalising compensation packages of employees. Also, the bigger issues like succession plan and dispute among the family members will be taken up by it.

Dr Rajnish Karki, who has devised the new organisational structure, said that the entire exercise is aimed at transforming the organisation into an ‘institutional state’. This is inevitable since a family-run concern will find it hard to handle the retail revolution happening in India. When the organisation grows, families have to gave way for the professional management.52

There are certain sporadic transformations in Chennai based companies also. One such transformation is in a Chennai based group companies, viz., Murugappa Group Companies. The following news was reported in a leading financial daily, Economic times.

“The Rs 3,100 crore Murugappa group has begun the hunt to select professional CEOs to turn the operations of the companies, with family members divesting their roles to assume functional responsibilities of the group.

Outlining the organisational changes initiated in the group, Mr M V Subbiah, chairman of the group and the new Murugappa corporate board (MCB), told reporters here on Monday that the major change would be the induction of three external professionals as non-whole time directors on the MCB. They will be top-level individuals with proven record in their profession and leadership qualities. Subbiah said that two of them have been identified one is a professor of Indian origin teaching abroad and the other a Chief Executive Officer working in an MNC. “We are waiting for their confirmation,” he said. The group is also in the process of selecting the third person. In all, the MCB

will have nine members. Five of them are senior family members Mr M V Subbiah is the chairman of the board with Mr M A Alagappan as vice-chairman. The others are Mr A Vellayan, Mr M M Murugappan, and Mr M M Venkatachalam and Mr Partho S Datta, who is the group president, finance. Mr Subbiah expected the full-fledged MCB to take off from the new-year. It will meet once in a quarter. The directors will act as “mentors” providing a link between the MCB and the statutory boards of the companies. Confirming the new-break, to The Economic Times, Mr Subbiah said the family members had already started handing over operational responsibilities to senior professional chief executives in various businesses and companies. All the members, including Mr Subbiah, will function from the IT House at Parry’s corner for better company-ordination and interaction. On the selection of the CEOs, he said, as far as possible it would be done from within the group “as they know the culture.” The mentor directors will be vice chairmen of the companies and provide inputs and suggestion to the professional team. There is no proposal holding the post of chairmen of the companies. Mr Alagappan will steer the group’s overall strategy while providing mentorship services to Tube Investments, IT Diamond Chain and the marketing services businesses. Mr Vellayan will address the group’s marketing thrusts, brand building, skills and systems while acting as a mentor for EID Parry and Coromandel Fertilisers. Mr Murugappan will drive the technology, including IT and research functions of the group and act as mentor for Carborundum Universal and plantations business. Mr Venkatachalam will be in charge of the group’s human resource functions and be a mentor for the group’s financial services (Cholamandalam Finance) besides Parry Confectionery. Mr Datta will focus on finance and financial restructuring. Mr Subbiah said the ‘Murugappa group is one of the big and well-knit joint families. We are all in he learning mode. We have decided to work together to meet the challenges and enhance the value for the stakeholders and customers. We spent lot of time and studied the working of the
other organisation before deciding to set up the MCB'. The group and its companies have done well. A number of them are number one or two in their fields. ‘But, they have to achieve superlative growth and profitability, maintain market leadership through technology and innovation and attract and develop high quality human resources,’ he said.\(^\text{53}\)

### 4.13 BOARD ROOM PRACTICES MODEL

The present researcher has constructed a model to measure the qualitative aspect of the functioning of a board. Ten factors are considered for developing such model which have been described in the first chapter. The board of each company taken for the study is measured with the help of this model. The total scores are ascertained for each company. The resultant scores of the different boards, as revealed by the model are given below table 4.38.

<table>
<thead>
<tr>
<th>Types of Board</th>
<th>Score</th>
<th>Number of Companies</th>
<th>Percentage of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Best</td>
<td>75 and Above</td>
<td>11</td>
<td>14</td>
</tr>
<tr>
<td>Good</td>
<td>50 and above and below 75</td>
<td>45</td>
<td>58</td>
</tr>
<tr>
<td>Poor</td>
<td>Less than 50</td>
<td>22</td>
<td>28</td>
</tr>
</tbody>
</table>

Source: Primary Data

On the basis of the above rating, 14 per cent of the companies have been rated as companies with best board practices and 28 per cent of the companies with poor practices. 58 per cent of the companies have been rated as the good board. Therefore, we can conclude that in majority of the cases, the boards of

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\(^{53}\) 'Murugappa board to have 3 External Directors, Hunt on for professional CEOs, Family Members to Divest Roles, Tuesday 2 November 1999. The Economics Times, Chennai edition.
listed companies in Tamil Nadu are good. Only 28 per cent of the companies are lagging behind.

**4.14 CONCLUSION**

The present chapter highlighted the rationale of the board and effectiveness of the unitary and two-tier board. An attempt has been made to classify the board on the basis of its functioning. The performance of the board has also been analysed from the angle of the board meeting. The various components of the board meeting like the duration of the notice given for the board meeting, agenda, minutes, attendance and the duration of the meeting were highlighted in order to ascertain how a board functions. Another major issue associated with the corporate management is the issue of insider and outsider. This boards of companies that are taken for the survey have also been studied from this angle. The composition of the board vis-à-vis the insider and outsider has also been ascertained. The necessity for having an independent board has also been highlighted and at the same time the factors which contribute to the independence of the board have been identified. The boards of the respondent companies had also been discussed on the basis of such factors. The Indian boards are in transition. From a family board, now it is transiting to a professional board. This phenomenon is noticeable in a countable number of companies. This transition had been sketched. Finally the researcher has constructed a model for measuring the board practices. On the basis of the model, one can classify the board into three categories - good, average and poor. This helps one in identifying the companies with good and bad board practices.