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CONCEPTUAL FRAMEWORK OF CORPORATE GOVERNANCE
CHAPTER-2

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CHAPTER 2

Conceptual Framework of Corporate Governance

2.0 Introduction

This chapter is including the conceptual Framework of corporate Governance and related terms.

In India, The question of corporate Governance has come mainly in the wake of economic liberalization, derequisition of Industry and business as also demand for a new corporate ethos and stricter compliance with the legislation. The new economic policy adopted by the Government of India since 1991 has necessitated the demand for introduction and implementation of a proper corporate governance policy in management of the companies not only in the interest of their stakeholders but also for the development of the economy.

Corporate Governance is the current buzzword in India as well as the world oven. It is practicing at every stage of company's affairs now days. Good governance is the expectations of shareholders in every walk of life these expectations are considered as right in corporate word. In India, though this word is new but fast growing. The good governance gives stress on two aspects, mainly (1) performance and (2) Accountability.

'Performance' in a sense & company on corporate leaders are supposed to contribute at the highest level of efficiency. This efficiency is expected but at the same time they are accountable for whatever has been carried out, every shareholder has right to know that what is wrong & what is right. Though corporate governance is totally new world for the corporate world but its acceptability is very high. Nowadays it is working in the every stage of company. Each corporate unit is expected to achieve maximum in the given time period, and unit is expected to use available resources optimum so that it can achieve goal efficiently.

'Accountability' means obligation to answer. Each corporate manager, leader & deportment is answerable and responsible to answer to the stakeholders.
Answerable in a sense what is the company’s performance, when it is moving? Where the resources are invested? Etc. This is because good governance demands greater accountability.

Corporate Governance has a unique role to pay to help attain the organizational goods in a smooth and uninterrupted manner amid all their entrepreneurial and business risks. The twin objectives of business enterprise to concentrate on profit earning as well as to conform to social responsibility performance fall within the ambit of corporate governance. Corporate governance is defined as the systematic and broad-based approach undertaken by an enterprise as a routine process to achieve the desired goals in a harmonized way with less of efforts and energy by giving due emphasis to the needs and aspirations of various parties having direct or indirect nexus with the enterprise. It is refers to the inbuilt and dynamic mechanism adopted by the corporate bodies to deal with their business activities in a compact, transparent and rebuts manner such that the varied interests of the several interactive parties like providers of capital, customers, creditors, government, society and the general public as a whole remain least disgruntled.

Corporate governance is not just corporate management; it is something much broader in approach to user in a fair, efficient and transparent administration to meet certain well-defined objectives. It is a system of structuring, operating, and controlling a business with a view to achieving long-term strategic goals to satisfy shareholders, creditors, employees, customers and suppliers, and complying with the legal and regulatory frame work, a part from meeting environmental and local community needs.

Corporate governance is a broad based approach in the overall business ambience to cover all the facades involved in the different operational activities carried on by business enterprises fortified with the moral and ethical values to best serve the different parties associated with the business organizations. Corporate governance is highly allied with the value creation in the organizational spheres for which a good degree of co-ordination is sought to be achieved at different levels of the organization to work together in a harmonious manner to protect the interests of the stakeholders. However, corporate governance, there is no ready-made 'Mantra' as such that can be safely applied to get the success; rather, it requires a value based
cultivation of corporate culture through the lens of the society. In the discloser on corporate governance practice, the emphasis is laid on social context and more specifically on the performance of social responsibility since business are the integral as well as inseparable part of the society whose social sanctions and patronage are inevitably required for their ultimate survival growth and prosperity.

A large variety of corporate activities like transparency in management, optimum and judicious utilization of search and valuable resources of the society, tax compliance, better employee management, protection of investors better financial disclosure for the stakeholders, protection from environmental pollution and degradation and the like fall within the ambit of corporate governance practice. The scope of corporate governance is broad-based having wide spectrum of interrelated and inter-connected activities in a harmonized and transparent way towards the effective achievement of organizational goals in a profound manner by laying greater emphasis on the corporate and social accountability of the business enterprises to the stakeholders in particulars and the society as a whole.

2.1 History of Corporate Governance.

Knowledge of the past can help to prevent firms and policy makers from repetition past mistakes. History is also like examples of how to do things right.

The roots of the word "governance" are traced to the word "gubernate" which means corporate governance would mean to steer an organization is the desired direction. The responsibility to steer lies with the Board of Directors and Governing Body. Governance is to do with the intrinsic nature, purpose, integrity and identity of an organization with spotlight on the entity's relevance, continuity and fiduciary aspects.

The pages of “Arthshastra ” written by Chankya and Kantilla speak highly about governance as back as thousands of years before Christ (BC) this Arthshastra maintains that for good governance, all administration, including the king were considered as the servants of the people. Good governance and stability were completely linked. There is stability that prevails only when leaders are responsive, accountable and removable. These basic tenets hold good even, today after 2010 years after christ's death (AD)²
According to Kautilya, the king gases fourfold duty namely "Raksha", "Vriddhi", "Palana" and "Yogakshema".

If one substitutes the 'state' by 'Corporation' then 'King' is the 'CEO' or the 'Board of Directors of a corporation' and the 'Subjects' are 'shareholders'. This similarity brings home the quintessence of corporate governance because central to the very concept of corporate governance is the strong belief that public good should be ahead of private good and that the corporation's reserves can hardly used for personal benefit. Let us touch four pillars of the four fold duty.

'Raksha' means protection and in corporate scenario it can be equated with the risk management dimension.

'Vriddhi' implies growth, and in the present day context can be equated stakeholder value enhancement.

'Palana' means maintenance or compliance. In present day situation it can be equated compliance to the law is letter and spirit.

'Yogkshema' implies well beings and according to chanakya it stands for social security system. In the present context it can be equated to corporate social responsibilities.

Chanakya's Arthshastra speaks of very strong self discipline for a king and the six enemies which a king should show and overcome are LUST - ANGER - GREED - CONCEIT - ARROGANCE and FOOLHARDINESS. In present context this set speaks of ethics aspects of business and personal ethics of the corporate leaders.

Corporate governance in Britain and the United States in the seventeenth, eighteenth and nineteenth centuries was for from perfect yet it was also for form being completely flawed. Anglo American corporate governance, therefore, offers both warning and lessons. In the eighteenth and nineteenth centuries, Americans and Britain's looked ask once at most forms of government regulation of business.

The international community has all along been supportive as evident of good governance practices as evident from various guidelines standards and codes
issued by various international agencies. Corporate governance is not a new invention but was inherent characteristic of all healthy organization even in the past.

2.2 Meaning of the Term Governance

According to 'world Bank'; Governance is... “The tradition and institutions by which authority in a country is exercised for the common good. This includes (I) the process by which those authority are selected, monitored and replaced (II) the capacity of government to effectively manage its resources and implement sound policies, and (III) The respect of citizens and the state for the institutions that govern the economical and social interaction among them.”

Governance is to do with the irrsintrinsic nature, purpose, integrity and identify of an organization with the fundamental focus on the entity's relevance, continuity, and fiduciary aspect.³

In common word, Governance means the way those with power use that power.

Governance is to control. Govern means direct and control and one can derive meaning as direction and control of affairs as governance.

2.3 Definitions of Corporate Governance.

When company follows corporate governance in practice in a way it becomes transparent in every single matter related to co.'s transactions, it has to be very honest while publishing financial information, firm has to fellow guidelines specified by various institutions and bodies.

♦ "Corporate Governance is about promoting corporate fairness, transparence, and accountability."
♦ "Corporate Governance is the system by which companies are directed and controlled."

–Cadbury Committee – U.K.

♦ According to ICSI (The Institute of Company Secretaries of India), - Corporate Governance is the application of best management practices, compliance of law is true letter and spirit and adherence to ethical standards for effective management and distribution of wealth and
discharge of social responsibility for sustainable development of
stakeholders."

- According to Mr. Monks and Mr. Minnow, – "Corporate Governance is the relationships among various participants in determining the directions and performance of a corporation."

- "Corporate governance is the way a company is organized and managed to ensure that all financial stakeholders receive their fair share of a company's earnings and assets." – Mr. Standard & Mr. Poor

- According to L.V.V. Layer,
- "Corporate governance can be defined as a set of system and processes which ensure that a company is managed in the best interests of all the stakeholders. The set of systems that help the task of corporate governance should include certain structural and organizational aspect; the process that helps corporate governance will embrace how things are done within such structure and organizational system."

- According to Dr. K. R. Chandratre.
- "Corporate governance is the expression which is not capable of precisely defined. However broadly speaking corporate governance denotes directions and control of the affairs of a company."

- Corporate Governance deals with laws, procedures, practices and implicit rules that determine a company's ability to take informed managerial decisions vis-a-vis its claimants - in particular, its shareholders, creditors, customers, the state and employees. There is a global consensus about the objective of good corporate governance maximizing long term shareholder value."

- CII (Confederation of Indian Industry)

- One other definition express, corporate governance has been defined as, a system of structuring, operating and controlling a company with specific aims of fulfilling the long term strategic goals of the owners, consider and care for the interest of employees, past and present, the needs of the environment and local community, maintain excellent
relations with both customers and suppliers, maintain proper compliance with all the applicable legal and regulatory requirements. 

The gist of all above definition can be reduced to the following words corporate governance is the accept are by management of the inalienable rights of shareholders as the true owners of corporation and of their own role as trustees on behalf of the shareholders. It is about commitment to values, about ethical business conduct and about making a distinction between personal and corporate funds is the management of the company. In fact strong corporate governance is almost indispensable to resilient and vibrant capital markets and is an important instrument of investor protection. It is the blood that fills the veins of transparent corporate disclosure and high quality accounting practices. It is the muscle that moves viable and accessible financial reporting structure. To put in short it is a system or the mechanism that functions like a watch giving time and hours, minutes, seconds and even fraction of second.

All above definition may also be defined as a system of structuring operating and controlling a company with the following specific aims:

(I) Fulfilling long term strategic goals of owners.

(II) Taking care of the interests of employees

(III) A consideration for the environment and local community.

(IV) Maintaining excellent relations with customers and suppliers.

(V) Proper Compliance with all the applicable legal and regulatory requirements.

2.4 Objectives of Corporate Governance

Corporate governance inspires and strengthens investor's confidence by ensuring company's commitment to higher growth and profits. It seeks to achieve following objectives.
(1) **Making Board to take independent and objective decisions**
A properly structured board capable of taking independent and objective decisions is in place at the helm of affairs.

(2) **Making the Board well balanced in terms of representation**
The Board is balanced as regards the representation of adequate number of non-executive and independent directors who will take care of the interests and well-being of all the stakeholders.

(3) **Making the Board to show more transparency**
The Board adopts transparent procedures and practices and arrives at decisions on the strength of adequate information.

(4) **The Board keeps well informed the shareholders**
The Board keeps the shareholders informed of relevant developments impacting the company.

(5) **The Board is an effective monitoring units**
The Board effectively and regularly monitors the functioning of the management team.

(6) **The Board Remain effective control agency.**
The Board remains in effective control of the affairs of the company at all times.

(7) **Making Board on Effective Machinery to Care for Stakeholders.**
The Board has an effective Machinery to sub serve the concerns of stake-holders.

The overall endeavor of the Board should be to take the organization forward, to maximize long-term value and shareholders; wealth.\(^5\)

### 2.5 Good Corporate Governance.

Good corporate governance practice is the essence of modern corporate management end over. Good corporate governance is the dexterity in management practice and is viewed like a good mother. As mother is to the new born baby, the good corporate governance is to the good corporate management. A good mother
takes care of the baby, trains her baby how to grow and live how to interact with the outer world and to tackle the situations finally teaches how to survive amid all adversities. A business enterprise in the similar way gets the requisite fervors and zeal through good governance practice to manage business affairs in a competent and fair manner to grow and prosper within the social boundary by paying adequate needs to the compliance of socio-economic rules and regulations, by observing transparencies in corporate activities and also by resorting to social responsibility performance to the best extent possible to ensure social justice, quit and appropriate in terms of both physical and financial magnitudes.

The essence of good corporate governance is to frame a system by which corporate bodies can be duly regulated and controlled, to ensure judicious sharing of rights and responsibilities among different participants - the board, managers, shareholders and other stakeholders - so as to perform business activities in a fair and transparent manner and also to augment corporate accountability in a social responsive manner by viewing and judging the business decisions through the lens of the society before their actual implementation in the business peripheries.

Good governance is important in every sphere of environment whether it be a corporate environment or general society or political environment. Good governance level helps improve social attachment and social recognition. When the resources are too limited to meet minimum expectation of the people, it is the pursuit of good governance that can help - promote the welfare of the society. A business organization gets the requisite vitality and potentiality to grow and survive amid all its shortcomings and hindrances provided a right dose of corporate governance is properly administered. There are glare of instances that many business organizations despite having sufficient profitability and amassing of wealth have been forced to defunct just for the sake of inadequacy in corporate governance in their overall organizational efforts and inefficiency in maintaining a transparent corporate management practice.

" The most penetrating Sarbane Oxley Act (Sox Act ) 2002 has to be highlighted. The sox Act is an Us Act enacted in the wake of the devastating Corporate failures that rocked the investors' confidence world wide and ushered on wide criticisms against the role of the company executives, directors and the auditors
for their gross negligence in safeguarding the interest of the different stakeholders. The world witnessed the appalling debacle of many prosperous US companies which were at the top of the list of investors' choice (like Enron, WorldCom, Xerox, etc). Despite having prosperity, these companies became victims of corrupt practices because of bad corporate governance, misuse of power by company directors and CEO that led to corporate disaster.  

2.5.1 Measures and Tools requirement for Good Governance.

When the resources are too limited to meet the minimum expectations of the people, it is the good governance level that can help to promote welfare of the society. The way forward to achieve the desired level in Indian scenario is to promote the social thinking in positive perspective along with the perfect monitoring mechanism of regulation framework. Below chart clearly shown effects of good governance.

**CHART-2.1**

**Effect of Good Governance**

- **Effects of good corporate governance**
  - **Stoke holders**
    - Investor Protection
    - Social Welfare
  - **Entrepreneurs**
    - Growth in Business
    - Better Goodwill

**Nation Overall Economic Growth**
2.5.2 Following are the measure of requirement for good governance.

1. Setting Internal Control System:

By setting internal Control Company can be ensure efficient conduct of business control leads to consciousness, which makes less possible chances of default.

2. Budgetary control:

When any transaction has been put under budgetary boundaries it leads to ensure accountability and transparency. Budget gives answers to no of questions, what has done? Why? And through which way? Thus it is base for planning and tool for control.

3. Financial planning and Management:

Scarcity of finance leads for crucial and critical management of financial resources, which requires in depth financial planning. Financial planning is concerned with rational acquisition and allotment of funds while financial management is concerned with optimum utilization of funds.

4. Compliance of Acts / Regulations:

Best governance that is follows norms. Every firm should / must follow all the related acts which are related with company's transactions. Acts includes standardization and norms that protects good will and resources.

5. Tax planning:

One or every firm has to plan in advance about all items of tax and how to pay it? They have to concentrate that how company will go for paying tax so that as far as possible it can take benefits. If tax is not paid in advance it leads to devaluation, Tax planning generates more shareholders return.

6. Management Information System:

Information is blood of business world. Company has to be in constant touch with environment through information. Management information system is channel of
inter related variables which has exact cause and effect relationship. It provides base for communication. Company maintains good governance through MIS. It can improve performance which is base for corporate governance.

7. **Cost Control:**

Cast is major aspect in profit. It cost is controlled it can stabilize or improve company's competitiveness. Every company needs to maintain its competitive value by controlling its cost. Cost control is best tool for good governance.

Above maintained tools can be considered as good governance practices.

2.6 **Factors Influencing Corporate Governance in Indian Companies.**

Numbers of factors affected to corporate Governance, Here summarized the factors which influence quality of governance in Indian Companies.

(a) **Integrity of the Management:**

A Board of the directors with a low level of integrity is tempted to misuse the trust, reposed by shareholders and other stake-holders, to take decisions that benefit a few at the cost of others.

(b) **Ability of the board:**

The collective ability, in terms of knowledge and skill of the board of directors to effectively supervise the executive management determines the effectiveness of the board. A board, which does not have members with right specializations, lacks this ability.

(c) **Adequacy of the process:**

Board of directors cannot effectively supervise the executive management if the process fails to provide sufficient and timely information to the board, necessary for reviewing plans and the performance of the enterprise. Similarity the process should be such that it should not dampen the entrepreneurial spirit of the executive management.
(d) **Commitment level of individual board members** :-

The quality of a board depends on the commitment of individual members to tasks, which they are expected to perform as board members.

(e) **Quality of Corporate reporting** :-

The quality of corporate reporting depends on the transparency and timeliness of corporate communication with shareholders. This helps the shareholders in making economic decisions and in correctly evaluating the management in its stewardship function.

(f) **Participation of Stakeholders in the Management** :-

The level of participation of stakeholders determines the number of new ideas being generated in optimum utilization of resources and for improving the administrative structure and the process. Therefore, an enterprise should encourage and facilitate stakeholders' participation.

## 2.7 Important Committees and Commissions On Corporate Governance.

Ever since the concept of corporate entity recognized, corporate governance in divergent manifestations has been in existence. The country of big corporations namely, US the foreign corrupt practices Act of 1977 (USA) made specific provisions regarding establishment maintenance and review of systems of internal control. In 1979, US securities exchange commission prescribed mandatory reporting on internal financial controls. Due to high profile failures in the US, the Treadway commission constituted in 1985 highlighted the need of putting in place a proper control environment, desirability of constituting independent boards and its committees and objective internal audit function. As a result, the committee of sponsoring organizations to a birth. It produced and stipulated in 1992,a control framework . After the Enron scandal in 2001, came other scandals involving large US companies such as world com, questions Global crossing and auditing lacunae that eventually led to the collapse of Andersen. These developments triggered another phase of reforms in the corporate area of corporate governance, accounts practices and disclosures - this time more comprehensive than ever before. In July 2001, less than a year from the date when enron filed for bankruptcy the Sarbanes Oxley Act - popularly known as SOX was enacted. This act made fundamental changes in virtually every aspect of
corporate governance in general and audition independence, conflict of interests, corporate responsibility enhanced financial disclosures and sever penalties for, credit default by manager and auditors, in particular.

In the late 1980's and early 1990's, a spate of scandals of financial collapse in the United Kingdom made the shareholders and banks work about their investments. This led the UK Government to recognize insufficiency of existing legislation and role of self regulation as a measure of controlling scandals and financial collapses. Some of the corporate disasters took place primarily due to insufficiency of implementable governance practices. To prevent the recurrence of such business failures, the Cadbury committee was set-up by the London stock exchange in May, 1991, interalia to help raise standards of corporate governance. 7

2.8 Recommendation of Different Committees on Corporate Governance


2.8.1 The Cadbury Report - 1992

The Cadbury committee was set-up in May 1991 by the financial Reporting council, the London stock exchange and the accountancy profession under the membership sir Adrian Cadbury and other members namely Ian Butler, Jim Butler, Jonathan Charkham, Hugh Collam, Sir Rom Dearing, Andrew Likieras, Nigal Macdonald, Milk Saurdland, Mark Sheldon, sir Andrew, Hugh smith sir Dermot de Trafford and others.

The terms of reference were: to consider the following issues in relation to financial reporting and accountability and to make recommendation on good practice namely;

(a) The responsibilities of executive and non executive directors reviewing and reporting on performance to shareholders and other financially interested parties ; and the frequency clarity and from in which information should be provided.

(b) The case for audit committee of the board, including their composition and role.

(c) The principal responsibilities of auditors and the extent and value of the audit.
(d) The links between shareholders boards, and auditors.

(e) Any other relevant matters.

➤ CADBURY COMMITTEE'S PROPOSALS.

The Committee's proposals are mutually supportive and should be taken as a whole. The code reflects existing best practice and fees of our recommendations require legislation. We believe that they will reinforce good corporate governance without shifting entire entrepreneurial initiative.

No system of corporate governance can be totally proof against fraud of incompetent. The test is how far such aberrations can be discouraged and how quickly they can be brought to light. The risks can be reduced by making the participants in governance process as effectively accountable as possible. The key safeguards are properly constituted boards, separation of functions of chairman and of chief executive audit committees, vigilant shareholders and financial reporting and auditing systems which provide full and timely disclosure.

Although the agent majority of companies are both competently run and audited under the present system of corporate governance, it is widely accepted that standards within the corporate sector have to be raised.

The way forward is through clear definitions of responsibility and acceptance by all involved that the highest standards of efficiency and integrity are expected of them. Expectations of corporate behavior are continuously rising and corresponding response is looked from shareholders, directors and auditors. The machinery is in place. What is needed is the will to improve its effectiveness.

This will involve a sharper sense of accountability and responsibility all record accountability by boards to their shareholders, responsibility on the part of shareholders to the Companies they own, and accountability by professional offices and advisers to those who rely on their judgment. All three groups have common interest in combining to improve the working of the corporate system.
[I] Compliance with the Code of Best Practice:

The boards of all listed Companies registered in the UK should comply with the Code of Best Practice set out on pages 58 to 60. As many other companies as possible should aim at meeting its requirements. Listed Companies reporting in respect of year ending after 30th June 1993 should make a statement about their compliance with the code in the report and accounts and give reason for any areas of non-compliance. Companies Statements of compliance should be reviewed by the auditors before publication. The review should cover only those parts of the compliance statement which relate to provisions of the code where compliance can be objectively verified. The auditing practices Board should consider guidance for auditions accordingly. All parties concerned with corporate governance should use their influence to encourage compliance with the code. Institutional Shareholders in particular shareholders committee, should use their influence as owners to ensure that the companies in which, they have invested comply with the code.

[II] Keeping the Code Up-to-Date:

The committee sponsor, convened by the financial reporting council, should appoint a new committee by the end of June 1995 to examine how for compliance with the code has progressed, how for our other recommendation have been implemented and whether the code needs updating. Our sponsors should also determine whether the sponsorship of the committee should be broadened and whether winder mother of corporate Governance should be included in is brief. In the meantime, the present committee will remain responsible for reviewing the implementation of its proposals.

[III] Director's Service Contracts:-

The companies Act should be amended to come into line with the requirement of the code that director's service contracts should not exceed three years without shareholders approval.

[IV] Interim reporting:-

Companies should expand their interim reporting to include balance sheet information. The London stock exchange should consider amending the continuing
obligation accordingly. There should not be a requirement for a full audit but interim reports should be reviewed by the auditors and the Audit practices Board should develop appropriate guidance - the according standard board in conjunction with Landon stock Exchange should clarity the accounting rules which companies should follow in preparing interim reports. The inclusion of cash flow information should be considered by the committee success or body.

[V] Enhancing the perceived objectivity of the audit:

Fees paid to audit firms for non-audit work should be fully disclosed. The essential principle is that disclosure should enable the relative significance of the company's audit non-audit fees to audit from to be addressed, both in a UK context, and where appropriate a word-side context. The 1991, regulation under companies Act 1956 should be reviewed and amended as necessary. The accountancy profession should draw up guidelines on the rotation of audit partners.

[VI] Enhancing the effectiveness of the Audit:

Directors should report on the effectiveness of their system of internet control and the auditors should report on their statement. The accountancy profession together with representatives of prepares of prepares of account should draw up criteria for assessing effective systems of internal control and guidance for companies and addition. Directors should state in the report and accounts that the business is a going concern with supporting assumption or qualifications as necessary and the auditors should report on this statement. The accountancy profession together with representation of prepares of accounts should develop guidance for companies and auditors. The questions of legislation to back the recommendation on additional report on internal control systems and going concern should be decided in the light of experience. The Government should consider introducing legislation to extend to the auditors of all companies the statutory protections already available to auditors in regulated sector (banks, building societies, Insurance and Investment business) so that they can report reasonable suspicion of fraud freely to the appropriate investigations authorities. The accountancy profession together with the legal procession and representative of the preparers of accounts should consider further the question of illegal acts other than fraud. The accounting profession should continue its efforts to
improve its standards and procedures so as to strengthen the standing and independence of auditors.

[VII] Voting By Institutional Investors:-

Institutional investors should disclose their policies on the use of their voting rights.

[VIII] Endorsement of work by other:-

The committee gives full support to the objectives of the financial reporting council and Accounting standard Board. It welcomes the action by the Financial Reporting Review pastel over companies whose accounts fall below accepted reporting standards. The committee supports the initiative of the Auditing practices Board on the development of an expanded audit report. It also gives it full support to the lead which it is taking in the development of auditing practice generally. The committee welcomes the statement by Institutional shareholders committee on the responsibilities of Institutional shareholders in the UK.

[IX] Issues for the committees Successor Body:-

Issues which the committees has identified that its successor body may wish to review or consider in greater depth include the application of the code to smaller listed companies; directors training; the rules for disclosure of directors remuneration, and the role which the shareholder could play; a requirement of inclusion of cash flow information in interim reports; and the procedures for putting forward resolution at general meetings. The committee and its successor will also keep watch on developments regarding the nature and extend of auditors liability.

[X] The Board of Directors

The board should meet regularly retain full and effective control over the company and monitor the executing management. There should be a clearly accepted division of responsibilities at the head of a company which will ensure a balance of power and authority such that no one individual has unfiltered powers of decision. Where the chairman is also the chief executive, it is essential that there should be a strong and independent element on the board with a recognized senior member. The board should include non-executive directors of sufficient caliber and number for
their views to carry significant weight in the board’s decisions. The board should have a formal schedule of matters specifically reserved to it’s for decision to ensure that the direction and control of the company is formally in its hands. There should be an agreed procedure for directors in the further are of their duties to take independent professional advice it necessary, at the company's expense. All directions should have access to the advice and services of the company secretary who is responsible to the board for ensuring that board produces are followed and that applicable rules and regulation are complied with. Any question of removal of a company secretary should be matter for the board as a whole.

[XI]  Non-executive Directors:

Non-executive directors should bring an independent judgment to bear on issues of strategy, performance, resources, including, key appointments and standards of conduct. The majority should be independent of management and force from any business or other relationship which could materially interfere with the exercise of their independent judgment apart from their fees and shareholding. Their fees should reflect the time which they committee to the company. Non-executive direction should be appointed for specified terms and reappointment should not be automatic. Non-executive direction should be selected through a formal process and both this process and their appointment should be a matter for the board as a whole.

[XII]  Executive Directors:

Directors service contracts should not exceed there years with out shareholders approval. There should be full and clear disclosure of directors’ total emoluments and those of the chairman and highest paid UK director, including provision contributions and stock options. Separate figures should be given for salary and performance related elements and the bases on which performance is measured should be explained-expenditure directors pay should be subject to the recommendations of a remuneration committee made up of wholly or mainly of non-executive directors.

[XIII]  Reporting and Controls:

It is the boards’ duty to present a balanced and understandable assessment of the company's position. The board should ensure that an objective and professional relationship is maintained with the auditors. The board should establish an audit
committee of at least three terms executive directors with written terms of reference which deal clearly directors should explain their responsibility for preparing the accounts next to a statement by the auditors about their reporting responsibilities. The directors should report that the business is a going concern, with supporting assumptions or qualification as necessary.  

2.8.2 GREENBURY REPORT OF 1995

This Report of the committee is popularly called the Greenbury Report. It included a code of Best Practices and its recommendation.

The Confederation of British Industry set up a group under the chairmanship of Sir Richard Greenbury. It was to examine the remuneration of the directors. Particularly compensation packages large pay increases and share options. The import recommendation was the establishment of Remuneration committee composed of Non-executive directors. The majority of the recommendations of the commnited were incorporated in the listing Rules of the London Stock Exchange.  

2.8.3 THE HAMPEL REPORT 1998

The committee was set up to review the extent to which Cadbury committee Report and the Greenbury committee Report had been implemented and whatever their purposes of recommendations were being achieved. The Hampel committee's recommendation and further consultations by the London stock Exchange become the combined code on corporate Governance.

2.8.4 THE TURNBULL REPORT

The original combined code required companies to include a narrative statement in their Annual Report of how in internal control provisions had been applied. However the combined cone did not have guidelines of how the provisions should be applied by the companies. This had to the establishment of a working group under the chairmanship of Niger Turnbull. The resulting Internal control Guidance for Directors on combined code was issued.
2.8.5 HIGGS REPORT, SMITH REPORT AND TYSON REPORT.

Following the review if the company law, a review of the combined code was commenced in July 2002. The subject was review of the role and effectiveness of non-executive directors. It was contacted by Derck Higgs (the Higgs Review). A group under the chairmanship sir Robert smith was setup to develop Guidance Audit committee in the combined code. The Tyson Report was commissioned on the recruitment and development of non-executive directors. All three provided recommendation for the revised combined code which emerged in 2003.12

2.8.6 COMBINE CODE ON CORPORATE GOVERNANCE 2008

The combined code on corporate Governance sets out standards of good practice in relation to issues such as board composition and development, remuneration, accountability and audit and relations with shareholders. All companies incorporated in the UK and listed on the main market of the London stock Exchange are required under the listing rules to report on how they have applied the combined code in their annual report and accounts.

(B) The Indian Counter - part

The initiatives taken by Government of India in 1991, aimed at economic liberalization and globalization of the domestic economy, led India to initiate reform process in order to the developments taking place work-wide. On account of the interest generated by Cadbury Committee Report, the Confederation of Indian Industry (CII), the Associated chambered and Industry (ASSOCIATION) and the Securities and Exchange Board of India (SEBI) Constituted committee to recommend initiatives in corporate Governance.

- Corporate Governance In India.

While the predominante from of C.G.es much closer to the East Asian insider model. There are a number of firms that resemble the Europeans version where the control is maintained through pyramidal from of ownership and control.
2.8.7 CII's Desirable Corporate Governance Code

Conferation of Indian Industry (CII) took special initiative on Corporate Governance, the first institution imitative in Indian Industry. The aim was to develop and promote a code for corporate Governance to be adopted and followed by Indian companies, whether in private or public sector, Banks or Financial Institution, all of which are corporate entities. The final draft of the send code was widely circulated in April 1997. In 1998 April the code was released. It was called Desirable Corporate Governance code.

There are in all 16 promendations in the connection which are briefly reproduced.

(I) The full board should meet a minimum of six times a great, preferably at an interval of two months and each meeting should have agenda items that require at least half a day's discussion.

(II) Any listed company with a turnover of Rs.100 cror and above should have professionally competent, independent, non-executive directors, who should constitutive at least 30 percent of the board if the chairman of the company is a non-executive director or at least 50 percent of the board if the chairman and Managing director is the person.

(III) No single person should hold directorships in more than 10 listed companies. This ceiling excludes directorship in 50 percent quite slake or associate companies where the group has owner 25 percent but not more then 50per cent equity stake.

(IV) For non-executive directors to play a material role in corporate decision making and maximizing long term shareholder value they need to: become active participants board such as the Audit committee; and know how to read balance sheet, profit and loss account cash-flow statements and financial ratio and have some knowledge of various company laws. This objective, excludes those who are invited to join boards as expert in other fields show as science and technology.

(V) To secure better effort from non-executive directors companies should. Pay a commission over and above the sitting fees for the use of the professional inputs. The per cent commission of 1 per cent of net profits if the company has a managing director-or 3 per cent-if there is no managing director; consider
offering stock options so as to relate reward to performance. Commission is reward on current profit. Stock options are reward contingent up on future appreciable at corporate value. An appropriate mix of the two can align a non-executive director towards keeping an eye on short-term profits as well as long term shareholder value.

(VI) While reappointing members of the board, companies should give the attendance record of the concerned director. If a director has not been present-absent with or without leave-of 50 per cent of more meetings from this should be explicitly stated in the resolution that it puts to vote.

(VII) Key information that must be reported to, and placed before the board must contain annual operating plans and budgets, together with up-dated long term plans; Capital budgets man power and overhead budgets. Quarter results for the company as a whole and its operating divisions or business Segments. Internal audit reports, including cases of theft and dishonesty of material nature; show cases demand and prosecution notice received from revenue authorities which are considered to be materially important-material nature if any exposure that exceed 1 percent of the company's net-work Fatal of serious accountants, dangerous occurrences, and any efferent or pollution problems; Default in payment of interest of non payment of the principal or any public deposit and or to any received creditor of financial institution Defaults such as non-payment or inter corporate deposits by or to the company, for goods sold by the company. Any issue which involves possible public or product liability claims of a substantial nature, including any judgement or order which may have either passed strictures on the conduct of the company, or taken an adverse view regarding another enterprise that can have negative implication for company. Details of any joint venture or collaboration agreement. Transaction that involve substantial payment towards good with, brand equity, or intellectual property. Recruitment and remuneration of senior offices just below the board level including appointment or approval of the chief Financial officer and the company secretary. Labor problems and their proposed solution. Quarterly detail of foreign exchange exposure and the steps taken by management to limit to risks of adverse exchange rate movement if material.

(VIII) It consists of seven sub clauses. Listed companies with either a turnover of Rs. 100 core or a paid up capital of Rs. 20 lakes should setup Audit committees.
within two years. Audit committees should consist of at least three members all drawn from a company's non-executive directors who should have adequate knowledge of finance, accounts and basic elements of company law. To be effective, the Audit committee should have clearly defined terms of reference and its member must be willing to spend more time on the company's work vis-a-vis other non-executive directors. Audit committee should assist the board to fulfilling its functions relating to corporate accounting and reporting practice, financial and accounting controls and financial statements and proposals that accompany the public issues if any security and thus provide of future supervision of the financial reporting process. Audit committees should periodically interact with statutory auditors and the internal auditors to ascertain the quality and veracity of the company's account as well as themselves. For Audit committees to discharge their fiduciary responsibilities with due diligence, it must be incumbent upon management to ensure that members of the committee have full access to financial data of the company its subsidiary and associate companies including data on contingent liabilities debts exposure, current liabilities loans and investments. By the fiscal year 1998-99, listed companies satisfying criteria (i) should have in place a strong internal audit department or an external auditor to do internal audits.

(IX) Under Additional shareholders information listed companies should give date on. High and law monthly averages to share prices in major stock exchange where the company is listed for the reporting year statement on value added which is total income minus the cost of all inputs and administrative expenses, Greater detail on business segments, up to 10 percent of turnover giving share in sales revenue review of operations analyses of markets and future prospects.

(X) Consolidation of group accounts should be optional and subject to the F/S allowing companies to leverage on the basis of the group assets and the income tax department suing the group concept is assuring corporate income tax if a company chooses to voluntarily consolidate it should not be necessary to annex the accounts of its subsidiary companies under section 212 of the companies Act. However, if a company consolidates, then the definitions of group should include the parent company and subsidiaries-where the reporting company owns over 50 per cent of voting state.
(XI) Major Indian stock exchange should gradually insist up on a compliance certificate signed by the CEO of or CFO of, which clearly states that. The management is responsible for the preparations, integrity and fair presentation of the financial statements and other information in the Annual Report, and which also suggests that the company will continue in business in the course of the following year. The accounting policies and principles conform to standard practice and where they do not, full disclosure has been made of any material departures. The board has overseen the company's system of internal accounting and administrative control systems either through its Audit committee for companies with a turnover of Rs. 100 crores or paid-up capital of Rs. 20 cores or directly.

(XII) For all companies with paid-up capital of Rs. 20 crores or more, the quality and quantity of disclosure that companies of GDR issue should be the norm for any domestic issue.

(XIII) The Government must allow for greater funding to the corporate sector against the security of share and other paper.

(XIV) It would be desirable for F/S as pure creditors to re-write their covenants to eliminate having nominee director expect in the event of serious are systematic debt default and incase of debtor company not providing six-monthly or quarterly operational date to the concerned F1(s).

(XV) This recommenders has four sub-points namely if any company goes to more than one credit rating agency then it must divulge in the prospectus and issues document the rating of all agencies that did such exercise. If is not enough to state the ratings. These must be given in a tabular format that show where the company stands relative to higher and lower ranking. It makes considerable difference to an investor to know whether the rating agencies placed the company in the top slots or is the idle or in the bottom. It is essential that we look at the quantity and quality of the disclosure in the USA and Britain if only to learn what more can be done to inspire confidence and create an environment of transparency.

(XVI) Companies that default on fixed deposits should not be permitted to accept further deposits and make inter corporate loans or investment until the default is made good and declare dividends until the default is made good.
2.8.8 Kumar Mangalam Birla Committee Recommendations\textsuperscript{14}

The securities and exchange Board of India (SEBI) set up committee under the chairmanship of Kumar Mangalam Birala on 7\textsuperscript{th} May, 1999 following CII's initiative to promote and raise standards of corporate governance. This report was the first formal and comprehensive attempt to evolve a code of corporate governance, in the context of prevailing conditions of governance is Indian companies as well as the state of capital markets at that time. The recommendations of Kumar Mangalam Birla committee, led to the inclusion of clause 49 in the listing Agreement is the year 2000. These recommendations are both mandatory and non mandatory.

- **The Constitutions of committee:**

The Committee has identified the three key constituents of corporate governance as the shareholders the Board of Directors and the management. Along with this the committee has identified major 3 aspects namely accountability, transparency and equality of treatment for all shareholders crucial to good corporate governance are the existence and enforceability of regulations relating to insider information and insider trading. These matters are currently being examined over here.

The committee had received good comments from almost all experts’ institutions, chamber of commerce A drain Cadbury - committee etc...

- **Corporate Governance Objective:**

Corporate Governance has several claimants - shareholders suppliers, customers, creditors, the bankers, employees of company and society. The committee for SEBI keeping view has prepared primarily the interest of particular classes of stakeholders namely the shareholders this report on corporate Governance. It means enhancement of shareholders value keeping in view the interests of the others stack holders.

Committee has recommended corporate governance as company's principle rather than just act. The company should treat corporate governance as way of life rather than code.
- **Applicability of the Recommendation**

**CHART -2.2**

**Applicability of the Recommendation**

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>Mandatory</th>
<th>Non-Mandatory</th>
</tr>
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</table>

The committee was of the firm view that mandatory compliance of the recommendations at least in respect of essential would be most appropriate in the Indian context for the present.

The committee felt that some of the recommendations are absolutely essential for the framework of corporate governance and virtually from its core while others could be considered desirable. Thus committee has classified recognize into two parts.

- **Applicability**

  The committee is of the opinion that the recommendations should be made applicable to the listed company them directors. Management, employees and professionals associated with such companies, in accordance with time table proposed in the schedule given later in this section.

  The recommendations will apply to all the listed private and public sector companies, in accordance with the schedule of implementation. As for listed entitles which are not companies, but body corporate e.g. private sector banks, financial institutions, insurance companies, pharmaceutical companies etc.. Incorporated under statutes, the recommendations will apply to the extent that they do not violate guidelines issued by prevalent authority.

- **Schedule of implementation**

  The committee recognizes that compliance with the recommendations would involve restructuring the existing board of companies.
With in financial year 2000-2001, not later than March 31, 2001 by all entities, which are included either in-group 'A' of the BSE on in S&P CNX Nifty index as on January 1, 2000, however, to comply with recommendation, these companies may have to begin the process of implementation as early as possible. These companies would cover more than 80% of the marker capitalization.

Within Financial year 2001-2002 but not later than March 30, 2002 by all the entities which are presently listed with paid up share capital of Rs.10 crore and above an net worth of Rs. 25 crore as more any time in the history of the company.

Within Financial year 2002-2003 but not later than market 31, 2003 by all the entities which are presently listed with paid up share capital of Rs. 3 crore and above.

- **Mandatory Recommendation**

- **Board of Directors:**

  An effective corporate governance system is one which allows the board to perform these dual functions efficiently. The board of directors of a company thus directs and controls the management of a company and is accountable to the shareholders. The board directs the company, by formulating and reviewing company's policies strategies, major plan of action , risk policy annul budgets and business plans, setting performance objectives, monitoring implementation and corporate performance and overseeing major capital expenditures, appositions and change in financial control and compliance with applicable law taking into the account the interests of the stakeholders.

- **Composition of the B.O.D. :**

  The composition of the Board is as important as it determines the ability of the board to collectively provide leadership and ensures that no one individual or a group is able to dominate the board. This has undergone a change and increasingly the board comprise of following groups of directors, promoter, director executive and non-executive directors, a part of who are independent.
I. Independent Direction:-

Independent directions are those directors who apart from receiving director's remuneration do not have any other material pecuniary relationship with company. Further all pecuniary relationship or transactions of the non executive directors should be disclosed in the annual report.

The committee recommends that the board of a company have an optimum combination of executive and non-executive directors with not less than fifty percent of the board comprising the non-executive directors.

In case a company has a non-executive chairman, at least one third of board should comprise of independent directors any in case a company has an executive chairman at least half of board should be independent.

1 Nominee Directors:

These directors are the nominees of the financial as investment institutions to safeguard their interest it may be present of retired employee of financial institutions on outsider. The committee recommend that institutions should appoint nominee on the board of companies only on a selective basis where such appointment is pursuant to a right under loan agreements as where such appointment in is considered necessary to protect interest of the institutions.

2 Chairman of the Board:

The committee recommends that a non-executive chairman should be entitled to maintain a chairman's office at the company's expense and also allowed reimbursement of expenses incurred in performance of his duties. This will enable him to discharge the responsibilities.

3 Audit Committee (Non Mandatory):

The committee is of the view that the need for having as audit committee grows from the recognition of the audit committee's position in the larger mosaic of governance process.

The audit committee's job is one of oversight and monitoring and carrying out this job it relies on similar financial management and our side
auditors. The committee believes that the progressive standards of governance applicable to the full board should also be applicable to the audit committee.

The committee therefore recommends that the board of a company should set up qualified and independent audit committee. The committee state the audit committee should have minimum three members, all being non-executive directors, with the majority being independent and with at least one director having financial and accounting knowledge.

4 Frequency of Meeting and Quorum (Mandatory Recommendation) :

The committee recommends that to begin with audit committee should meet at least thrice a year. One meeting must be held before finalization of annual accounts and one necessarily every six months. The quorum should be either two members or one third of members of audit committee, whichever is higher and there should be a minimum of two independent directors.

5 Powers of audit committee (Mandatory) :

(1) To investigate any activity within its terms of reference.
(2) To seek information from any employee.
(3) To obtain outside legal on other professional advice.
(4) To secure attendance of outsider with relevant expertise, if it considers necessary.

6 Functions of Audit Committee (Mandatory) :

(1) To ensure that the financial statement is correct, sufficient and creditable.
(2) Recommending the appointment and removal of external audit.
(3) Reviewing with management annual financial statement before submission to board related to changes in accounting policies and practices.
   (a) Major accounting entries.
   (b) Qualification in draft audit report.
   (c) Significant adjustment arising out of audit.
   (d) Compliance with accounting standards.
   (e) Compliance with stock exchange and legal requirement concerning financial statements.
Any transaction that may have potential conflict with the interest company at large.

Reviewing with the management about adequacy of Control.

Discuss with internal auditors in to the matter suspecting fraud on irregularity.

Discuss with external auditors before the audit commences and also post-audit discussion to ascertain any area of concern.

- **Remuneration Committee (Mandatory):**

The committee is of the view that a company must have a creditable and transparent policy in determining and accounting for the remuneration of the directors. For this purpose the committee to determine on their behalf and on behalf of the shareholders with agreed terms of references. The Remuneration committee should comprise of at least three directors, all of them should be non-executive directors, the chairman being an independent one. The chairman of Remuneration committee should present at AGM. It is important for the shareholders to be informed of the remuneration of the directors of the company, which is mandatory.

2.8.9 **NareshChandra Committee Report on Corporate Governance**

The Government of India in response to these international developments especially the audit-company relationship set-up a committee to look into the issues relating to auditor-company relationship, such as rotation of auditors / auditing partners, restriction on non audit work/fee, procedures for appointment of auditors, determination of audit fees, the role of independent directors and disciplinary procedures for accountants. The committee submitted its report in February 2003 and some of the required changes were implemented through the changes in the listing Agreement.

According to the committee, the statutory auditor in a company is the "lead actor" in disclosure front and this has been emply recognized sections 209 to 233 of the companies act. The chief aspects concerning the auditors functioning as per the act are:

Auditors are fiduciaries of the shareholders not of the management as they are appointed as the shareholders appoint them.
* Auditor's independence id guaranteed as rules for removing on replacing an auditors as more stringent than for reappointment.

* The statutory auditor of a company can, at all time, have the right of access to all books of accounts and vouchers of a company and his repeat can be quite exhaustive to specify whether.

* The auditors could obtain from management all information and explanations that were necessary for the purpose of audit.

* Proper books of accounts have been kept by the company.

* Brained offices have been audited by him.

* Company's accounts conform to accounting standards set by the institute of chartered Accountants of India.

➤ **Some Mandatory functions are as under:**

* The adequacy of internal control commensurate to the size of the company and its business.

* The adequacy of records maintained on fixed assets and inventories and whether any fixed assets were re-valued during the year.

* Loan and advances that were given by the company, and whether the parties concerned were regular in repaying the principal and interest.

* Loans and advances taken by the company and whether these were at terms in judicial to the interest of the company and also whether these were being property repaid according to conducted schedules.

* Transactions including loans and advance with related parties as defined by section 301 of the companies act.

* Fixed deposits accepted by the company from the public and if so whether these conform to the provisions laid down by section 58 A of company's Act.
* Regularity of depositing of provident fund dues and whether the employees state Insurance Act. 1948 was applicable to the company.

* No personal expenses of directors and employees were charged to the profit &loss A/c.

* In the case of any manufacturing company, whether the management has confirmed to the manufacturing and other companies order 1988.

➤ Guidelines of Committee to Auditors:

(i) For the public to have confidence in the quality of audit, it is essential that auditors showed always be and be seen to be independent of the company, which includes integrity, professional ethics and objectivity.

(ii) Before taking any work auditor must consider that there should not be any threat to his independence. And it present he should adopt risk aversion virtue.

(iii) Where such treats exist the auditor should either desist from the task or, at the very least, but in place safeguards that criminate them to reduce the threats to clearly insignificant levels.

For the auditor is unable to fully implement credible and adequate safeguards then he must not do the work.

2.9 Ethical Principle of Corporate Governance

Ethics is a normal science dealing with "What is right?" and "What is wrong?" and "What is good?" and "What is bad?" when we come to business ethics, it is a form of applied ethics. In a board sense ethics in business is simply the application of moral or ethical norms to business. Ethics is a set of principles or standards of human conduct that govern the behavior of individuals or group in that sense-organization. Using these ethical standards, a person or a group of persons or an organization regulate their behavior to distinguish between what is right? And what is wrong? As persuade by others.

Ethics can be defined as the discipline dealing with moral duties and obligation, and explaining what is good or not good for others and for us. Ethics is the
study of moral decisions that are made by us in the course of performance of our duties. Ethics is the study of characteristics of moral and if also deals with truth and justice, concerning a variety of aspects like the expectations of the society fair competition, public relation social responsibilities and corporate behavior.

Business ethics encompasses the principles and standards that guide behavior in the conduct of business. Business must balance their desire to maximize profit against the need of stake-holders. Maintaining this balance often calls for trade-offs. To address these unique dimensions of businesses rule-articulated and implicit, are developed to guide the business to earn profits without harming individuals or society as a whole.

From management prospective an ethical decision is one that reasonable or typical stakeholders would find acceptable. In contract an unethical decision is one that managers will try to hide because that decision is one that benefits one or group of stakeholders at the expense of society or other stakeholder. There are a wide range of unethical practices ranging from corruption, cooking books to deceive all shareholders and investors. Having parallel book and operating in the black-market resulting in losses to many stakeholders, especially the minority shareholders, damaging the environment, treating employee badly or distributing unsafe products to customers.

These unethical practices in an organization can be very expensive both in terms of financial costs and is the loss of the organizations reputation with all stakeholders.

There are countless example of bad ethical behavior on the part of corporate world. Hear let us takes only a few cases. A classic example is the Bhopal gas tragedy, where in 1984, over 3000people died over-might when there was a leak of methyl is Ocymide from Union carbide plant, while there is some controversy over the responsibility for the accident, the facts are that this plant. Under these circumstances as purely economic consideration might dictate various cost cutting measures were in place. These measures included decreased maintenance expenses, and substantial reduction of qualified workers. Instead of original train operators per shift there were six. In addition, there are suggestions of sabotage from disgruntled
employers Mr. Troffer, Mr. Day and Mr. Love in 1989. All he cost reduction measures made from an economic standpoint, and certainly the manager is Union carbide both India and in the US did not want -the Bhopal accident to occur. However, what stands out is a failure to look beyond the economic standpoint and consider whether the cost savings were being obtained at too high a risk to the community.\(^\text{15}\)

Through the Bhopal gas disaster has the divisions’ distribution of being the world’s worst individual disaster such cases frequently come up world-wide. In the Manville Corporation, an asbestos company was aware about the health hazards its workers increased by breathing the asbestos dust, but supposed that information from them for 40 years. the company calculated that the cost of improving cost of paying for health insurance and allowed hundreds of workers to get lung cancer. When this finally came out in the open the consequence was negative for Manville. From being among the top U.S. companies, it had to file for bankruptcy protection. As in the case of Union carbide, it is unlikely that the managers were immoral people. But as is the case of Bhopal disaster they did not consider the implications of its economic decisions on other stakeholders.

The purpose of business ethics is not to change the basic values of an employee or to educate them on moral standard, but the purpose of business ethics is to remind managers that business decisions have moral dimensions and to prompt them to consider the implications of economic decisions on all stakeholders. Such a mindset created is an organization that forests an ethical climate. The most significant impact on the ethical climate of an organization is the top managers. To successfully create an ethical climate in an organization, two things are very important.

(i) People should perceive the manager as a moral person; this is determined by who they are and what they do. These they act as role models.

(ii) Managers are to take action that foster the ethical climate-they need to communicate regularly about ethics and values and use a reward system that holds every one accountable to values and standards, rewards are dangerously powerful tools and need to be cased extremely with percentage on case and caution.
The goal of business ethics is more to help people think the moral and social implication of business decisions, every business society has its accepted behaviors if someone deviates from, it is considered to be unethical. Business communication showed gets its accepted behavior written down and codified.

The corporate should periodically revise its rooms and impinge on its members to adhere to these.

**How to build ethics?**

**CHART – 2.3**

**Ethics of Corporate Governance**

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Stake Holders
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Customers Employees Investors Competitors Suppliers Society

2.9.1 Principles or Ethics for Stakeholder:

This means how bus organization should deal with different stakeholders like....

(A) **Principles/Ethics toward employees:**

- Provide such wages and compensation that improve worker's living condition.
- Provide such work environment that maintains health of employees.
- Try to be honest with employees during communicating them.
- Try to consider idea, suggestions & complaints of employees.
- Protect employees.

(B) **Principles/Ethics toward investors:**

- Apply Professional and diligent management for fair management.
- Disclosure of all information
- Conserve/prefect and increase investors assets.
Respect Suggestions & Complaints of them

(C) Principles/Ethics toward Suppliers:—

- To be fare in pricing
- Pay in time accordance with terms
- Proper supplier who gives preference to human dignity.
- Share information
- Maintain relationship with supplies

(D) Principles/Ethics toward communities:—

- Respect human rights.
- Support govt. & public policies.
- Promote development in society.
- Respect culture
- Maximize charity if possible

(E) Principles/Ethics toward Customers:—

- Provide highest quality product.
- Treat customer fairly.
- Provide reasonable price.
- Provide all knowledge to customers related to product.

Company should followed all these ethics so that it can reduce risk of not following ethics.16

2.10 Company law Related to Corporate Governance

The companies Act, 1956 was enacted on the recommendations of the Bhabha Committee set-up in1950 in order to consolidate the existing corporate laws and provide a new basis for corporate operation in independent India. The companies Act, 1913 was repealed with the enactment of this law in 1956. Since 1956 till date, a constant need for streamlining of the Act was felt from time and again as the corporate sector grew in pace with the growth of Indian economy. As many as 24 amendments to this Act were made since 1956. Major amendments took place by way of companies (Amendment) Act, 1988 after considering the recommendations of the Sachar committee, followed by further amendments in 1998, 2000 and 2002. The
latest amendment was made through the companies (second Amendment) Act, 2002 after considering the report of Irani committee.

India took up its economic reforms program in the 1990s. Again a need was felt for a comprehensive review of the companies Act, 1956 which has become the bulkiest and archaic with 781 sections by this time. Three unsuccessful attempts were mad in 1993, 1997 and then in 2003 which contained several important provisions relating to Corporate Governance was withdrawn by the government in anticipation of another comprehensive review of the low. However, there is no denial of the fact that that in today’s fast, competitive and technology driven business environment while on the one hand, Corporate require greater autonomy of operation and opportunity for self regulation with optimum compliance cost, there is also a need on the part of company promoters, directors and managers to bring trans piracy through better disclosures and exhibit a greater responsibility for improved compliance of corporate governance principles, code of best practice, and protection of interest of the investors and stakeholders, on the other.

The central government has taken a fresh initiative once again and released a concept paper on company law in 2004 seeking comments and suggestions from a large number of organizations, professional bodies and individuals. There after The government thought it prudent to get all these comments and suggestions evaluated on their merits by an independent export committee was constituted on December 02, 2004 under the chairmanship of Dr. J.J. Irani, with 13 members and 6 special invitees drawn from various disciplines including trade and Industry, chambers of commerce professional institutes, banks and Financial institutions, senior advocates, government ministries as well as regulatory bodies. The object of this exercise has been to fulfill the desire of the government to have a simplified modern company law which can address the on going changes in the national and international scenario, enable adoption of internationally accepted best practices and provide flexibility for timely evolution of new arrangements in response to the requirements of ever changing business models. The committee submitted its report on May 31st, 2005 to the Hon'ble Minister for company Affairs for consideration.
2.11 SEBI Guideline for Corporate Governance

The SEBI appointed a committee on corporate Governance on 7\textsuperscript{th} May, 1999 under chairmanship of Shri Kumar Mangalam Birla to promote and raise the standard of corporate Governance with specific terms.

SEBI introduce a new clause - 49 in the Listing Agreement in the year 2000, specifying the principles of corporate governance to be followed by the listed companies. Thereafter, SEBI in corporate various committees' recommendations in clause 49 and revised it seven times within the period 2000-2005. The latest and revised clause - 49 of listing Agreement has been introduced in 29\textsuperscript{th} October, 2004. Moreover as many as twenty-four amendments to the companies Act were made since 1956 till date, of which at least three amendments pertaining to corporate governance were made during the period 1999, 2000 & 2001. The committee identified three Key constituents of Corporate Governance as the shareholders. The Board of Directors and the management specifying their and responsibilities as against their right in the context good corporate governance\textsuperscript{18}. The main hitting points were accountability, transparency and quality of treatment for all stakeholders.

The SEBI Board considered the recommendation of the committee and decided to make the amendments of listing agreement is pursuance of the decision of the Board and a new clause in the listing agreement in February, 2000.\textsuperscript{19} This clause 49 has been amended in Gene with dynamic market with a view to improve the standards of Corporate Governance.

According to SEBI, The companies have to submit compliance status on eight sub-clauses:\textsuperscript{20}

1. Board of Directors  
2. Audit Committee  
3. Shareholders/ Investors' Grievance Committee.  
4. Remuneration of Directors  
5. Board Procedure  
6. Management
7. Shareholders and
8. Report on Corporate Governance

2.12 Agency Theory

The distinction between ownership (shareholders) and control (Mangers) arises in view of the widespread dispersion of ownership, which was pointed out by Berle and means in 1932. The agency problem exists because managers might misuse their position and there are costs associated with prevention of abuse. Corporate governance has to subordinate managers' interest to that of shareholders. Since shareholders are residual claimants they have the greatest incentive to ensure the success of the corporation. Michael Jensen, the proponent of agency theory stresses the efficiency of capital market as a disciplinary mechanism, generating optimal assets prices. According to this view the market for corporate control is a fast and efficient mechanism by which firms are forced to exit mature markets where over capacity persists, capital market discipline assures timely exit from low tech sectors in which importance of organizational skills is likely to play only a minor role.

2.13 Report on corporate governance

Report on corporate governance giving the following information.

(a) A brief statement of company's philosophy on the code of governance

(b) Board of Directors composition number of meetings, attendance of each Director, other committee meetings, date of last Annual General meeting etc.

(c) Audit committee - composition, terms of reference, meetings and attendance.

(d) Remuneration committee-composition, terms of reference, meetings and attendance

(e) Shareholders committee-names of non-executive Directors heading the committee, name and designation of compliance officer, number of complaints received number of complaints solved and pending, and pending share transfers.
(f) General body meetings, location and time where last 3 AGM, held, whether special resolutions were put through postal ballot last year, details of voting pattern, person who conducted the postal ballot exercise and procedure adopted.

(g) Other disclosures like significant related party transaction, penalty and strictures imposed on the company by stock exchange or SEBI.

(h) Means of communication-details of half yearly Reports sent, quarterly results sent, newspaper in which published.

(i) General shareholder information-date, time and venue of AGM, financial calendar, date of book closure dividend payment data, stock code, market price date, register and transfer agent details, distribution of shareholding, outstanding GDRs ADRs and warrants, plant location address for correspondence.

(j) Auditors certificate on corporate governance should also form part of Directors Report of such listed companies.

2.14 Key Governance parameters.

The various committees Report on corporate governance have been explained in number of parts. In this research an attempt has been to highlight some of the committee's view and recommendations related to corporate governance issues. It is Important to mention that the committee's recommendations for convenience of analysis. Thus researcher want to explained the various parts of the corporate governance report of pharmaceutical companies and ascertain the actual position with respect to the following key governance parameters.

2.14.1 [A] Various Committees on C.G

1. Code of conduct

There should be written code of conduct for senior financial personnel including chief Financial officer, Treasurer and Financial controller. It is obligatory for Borad to define a code of conduct for senior management not just senior financial personnel. the report on Corporate Governance (1999) observed that management
should be subservient to the Board and must operate within the boundaries and the policy framework laid down by the board. While the board is responsible for adherence and enforcement of principles of corporate governance the real onus of implementation lies with the management. The role of management should be clearly defined to ensure the translation into action, the policies and strategies of the board and implementing the directive of the board to achieve corporate objectives framed by the board.\textsuperscript{21} It is imperative that organizations explicitly prescribed norms of ethical practices and code of conduct are communicated to all the stakeholders are clearly under stored and followed by each member of the organization systems should be in place to periodically measure, evaluate and if possible recognize the adherence to code of conduct.

To encourage ethical behavior most of the companies have come-out with corporate code of conduct such codes service as important guideline for people in the organization, code of conduct cover different and relevant aspects of behavior how should employees to be treated or customers on other stakeholders, some codes of conduct specify the company's position about giving or remaining gifts and hiring of relations or friends.

2. Board of Directors / Board Issues.

The three trio of corporate governance are board of directors, management and shareholders. While each of them has important responsibilities of its own, it is their interaction with each other’s that is the key to effective governance. In tandem they constitute an effective set of checks and balances. The system can become unbalanced if any one of them is not functioning well. The relationship in the governance triangle consisting of Board of Directors-Management, Management-Board of Directors and Board of Directors-shareholders depend on mutual accountability and responsibilities. The Board lays down policy and strategy and monitors the performance and counsels the management. The Board hires and fires and through the Remuneration committee sets the compensation for the CEO. It may be noted that in USA the jobs of CEO and chairman are usually combined while in India the practice varies. In some they are held by different individuals while in others they are combined, sir Adrian Cadbury believes that the job of chairman and chief executive demand different abilities
and perhaps temperaments. In his opinion it is very much in shareholders’ interests to ensure they are performed by different people.

♦ **Building an Effective Board**: Good boards which are involved, diligent value adding do not emerge from structural changes. Exemplary boards are robust, effective social systems. All the Board members should get adequate information. If the board is healthy the CEO provides adequate information on time and trusts the board not to meddle in day operation. He should not see the Board as an obstacle to be managed.

♦ **Trust and Candor**: The chairman and other board members should build trust by sharing reports / information on time for them to read. Board members should be encouraged to spend time together, meeting key company personnel and visiting sites. Polling individual members occasionally by an outside agency can uncover if factions are forming or if members are uncomfortable with an autocratic chairman.

♦ **Open Dissent**: The respect and trust should make Board members feel free to question each other assumptions and beliefs. Dissent is not the same thing as disloyalty. Dissent is the best insurance against crossing ethical divide among board members. Wrong doing will be challenged. Board members should not be deferential. While we cannot legislate of mandate ethical behavior, an environment whereby honesty and fairness is paramount can be fostered. If integrity is to be the foundation for competitiveness it has to begin at the level of the board. Highest performing companies have extremely contentious boards that regard dissent as an obligation and treat no subject as undiscussable. If directors differ / dissent they should be enabled to give an independent report to shareholders backed by adequate justification. Record of voting on board resolution should be available for information of shareholders.

♦ **Fluid portfolio of Roles**: members of the board should be encouraged to play a variety of roles which gives directors a wider view of business and the alternatives before it.
Individual Accountability: peer pressure is the best enforcement mechanism. Members of the board should be given tasks about strategic and operational issues the company faces to be reported to the board.

Independent Directors

The Report on corporate governance has defined independent director as a director and the independent director as a non-executive director of the company who:

✔ Definition of Independent Director as a Director

- not receiving remuneration
- not related to promoters or management
- not an executive of the company in the last three years
- not a partner or executive in the auditing firm not a significant supplier or vendor or customer
- not a shareholder owning 2% or more
- not been a director for more than 3 terms of 3 years each

✔ Definition of Independent Director as a non executive

- A part from receiving remuneration does not has any material pecuniary relationship or transaction with the company.
- Is not related to promoters or management
- Has not been an executive of the company in the preceding 3 years
- Not a part or an executive of the statutory audit firm or internal audit firm that is associated with the company.
- Is not a supplier, service provider or customer of the company.
- Is not shareholder owning 2% or more of shares of company.

✔ Role of Independent Directors.

Director or Independent Director: non-executive director is typically a powerful business person in his own right whose wisdom is based on a clean understanding of today's financial issues and a grasp of How create shareholders value. The modern nonexecutive Director frequently represents the larger shareholders within the company. Today's larger shareholders have
shown that they wish to see board decisions taken of which they fully approve. This is the global trend and has found acceptance in India. SEBI also emphasizes the importance of non-executive, independent directors by insisting upon committees of Directors directly or indirectly to play a major role in controlling the audit committee and remuneration committee, which consists of only independent Directors should be prepared to "Whistle blow" or even resign where companies are not willing to address to the concern raised on behalf of the shareholders. Independent Director should there to help the executives, build success, not to police the rest of the Board. They are the shareholders special watchdog.

3. Board Committees:

(A) Audit committee

The law requires that every registered company (a listed company has wider obligations) should be audited annually by a firm of independent accounts. The audit process is stipulated in the case of listed companies to ensure the confidence required for the capital markets to operate effectively. Audit provides the basis for public trust that audited financial statements provide an accurate picture of the company's finances.

❖ Role of Audit Committee.

Audit committee plays an important role in the wider governance process through oversight of financial reporting. It provides oversight of the company's internal and external auditors, approving their appointment and dismissal, reviewing and approving audit scope and frequency, receiving their reports and ensuring that management is taking appropriate corrective action in a timely manner to address control weaknesses, non compliance with policies, laws and regulations and other problems identified by auditors.25

All the committee that reported on reform of corporate governance envisage that all the three directors (minimum membership) of the audit committee should be independent directors which would render the role of audit committee effective and serve useful purpose. The three groups consisting of the full board including the audit committee, financial management including internal auditors and
external auditors ensure responsible financial disclosure and active and participatory oversight. Auditors and accountants are the first outsiders to know if something is amiss in a company.

*They are the shareholders' watch dog.*

The audit committee has to ensure active and independent oversight of financial reporting. It has to evaluate management effectiveness internal control mechanism and risk management and risk containment policies. The committee relies on internal and external auditors for monitoring and surveillance. The audit committees oversight has to ensure appropriateness of company's accounting policies and the rigorous of internal controls including management controls. The audit committee has to meet once every quarter and interact with both internal and external auditors.26

![Seven Principles to Govern Audit Committees](image)

The seven principles indicated by the US conference Board commission on public trust and private Enterprise (CPIPE), 2003. These are equally relevant in India and are stated here

[1] **Compliance**

Audit committees should be vigorous in complying with the requirements that members of audit committee must be independent and have both knowledge and experience in auditing financial matters. The audit committee is also responsible for the appointment, compensation and oversight of the work of auditors. and that the outside auditors report directly to the audit committee.

**Best Practices:** Board should devote sufficient resources and time to implement audit committee's requirement. Board of directors should assess the independence and qualifications of members of audit committee. The company has to disclose whether the committee includes a financial expert. Audit committees should conduct annual assessment of the performance of the committee and its members.

[2] **Audit committee Education:**

Members of the audit committee should participate in an initial orientation program upon appointment to the committee as well as education programs later.
[3] **Risk**

Public companies should revise their internal controls to reflect a board risk-based approach and to support to certification process for both financial reports and internal controls. Effective internal control systems should be designed to encompass all major areas of risk and vulnerability in a company's operation, including corporate governance issues. According to CPIPE evaluation of the company's overall risk environment should include an analysis of overall risk environment should include an analysis of overall risk environment and controls and information systems that address these risk. The survey of corporate directors conducted by institute of internal Auditors (USA) found that 50% of directors indicated that their companies did not have in place effective risk management system.

**Best Practices:**

- All companies should have an informal audit function.
- An audit plan centered on corporation's risks and vulnerabilities should be prepared for review and approval by audit committee or board
- Internal auditors should have a direct line of communication and reporting responsibility to the audit committee and attend audit committee meetings.
- Every company board especially the audit committee should make enterprise risk assessment and internal controls high priorities.

[4] **Auditor Rotation**

Audit committees should consider rotating audit firms when there is a combination of circumstances that could call into question the audit firm's independences from management.

[5] **Professional Advisors for the Audit Committee:**

The audit committee should if necessary, retain professional advisors with no other ties to the company in carrying out its functions.
[6] Services Performed by Accounting Firms

Public accounting firms should limit their clients to performing audits and to providing closely related services that do not put the auditor in an advocacy position such as novel and debatable tax strategies and products that involve income tax shelters and extensive off shore partnerships or affiliates.

[7] Business Model of Accounting Firms:

Accounting firms should each examine their business model to ensure that the model is consistent with the idea that quality audit is their number one priority.27

(B) Remuneration Committee.

The remuneration committee set-up by the board should determine the company's policy on specific remuneration packages for executive directors including pension rights and compensation payment. The committee has overall responsibility for approving and evaluating the executive directors and senior management compensation plans. Policies and Programs of the company. The compensation committee of three members is appointed by the Board on the recommendation of the nomination committee. The compensation committee is responsible for administering stock option plans including the review and grant of eligible employees under the plan.

The committee on corporate Governance (1999) was of the view that a company must have a credible and transparent policy in determining and accounting for the remuneration of the directors. The policy should avoid potential conflicts of interest between the shareholders. The directors and the management. The over riding principle in respect of directors' remuneration is that of openness and shareholders are entitled to a full and clear statement of benefits available to the directors.

For this purpose the committee recommended (non-mandatory) that the board should set-up a remuneration committee to determine on their behalf and on behalf of the shareholders with agreed terms of reference. The company's policy on specific remuneration packages for executive directors including pension rights and any compensation payment.28
The committee however recognized that the remuneration package should be good enough to attract, retain and motivate the executive directors of the quality required, but not more than necessary for the purpose. The remuneration committee should be in a position to bring out objectivity in determining the remuneration package while striking a balance between the interest of the company and shareholders.

❖ Seven Principles to Govern the Remuneration committee

The (US) conference Board CPIPE (2003) has determined seven principles to govern the remuneration committee which are of relevance.

[1] Responsibilities:

Remuneration committee should take primary responsibility for ensuring that the compensation package to management through cash pay, stock and stock based awards are fair and appropriate to attract retain and motivate management and are reasonable in view of company economics and of the relevant practices of other similar companies. The remuneration committee should consist of independent directors.

[2] Performance Based Compensation:

Performance based compensation tied to specific goals should be encouraged in a balanced and cost effective manner. The compensation committee should adopt specific policies and programs to recapture in incentive compensation from executives in the event that malfeasance on the part of such executives results in substantial financial harm to the corporation.

[3] Equity Based Incentives:

Equity based compensation should be used in a reasonable and cost effective manner. It is a desirable method in start-up companies with little cash, in industries where it is accepted as part of compensation package or where an important portion of intellectual capital resides with employees.
[4] **Long-term Focus:**

Remuneration policies should confer a financial stake through long-term acquire and hold practices by key executives while ensuring that the cost of creating that stake is reasonable and cost effective. Senior management should be required to accumulate meaningful amount of company stock on a long-term basis with a minimum holding period.

[5] **Accounting Neutrality:**

Compensation decision should be related to goals and relative costs rather than simply on their accounting treatment. To eliminate accounting bias in favor of one form of equity based compensation, fixed price stock options should be expensed on financial statements of public companies.

[6] **Shareholders Rights:**

Shareholders should have control over potential equity dilution resulting from remuneration packages. The plants should be approved by shareholders.

[7] **Transparency and Disclosure:**

The interests of the market and shareholders are the best served if the disclosure of executive compensation and the economic impact is transparent and readily understandable. Disclosures should include a statement showing earnings per share after dilution and the proportion of future shareholder value that equity based compensation plans would provide to executives and employees. A company’s disclosure should include a summary in plain English of the significant terms of the agreement when the agreements are filed with regulatory authorities.

(C) **Nomination committee:**

OECD principles suggested that boards may consider establishing a nomination committee with a minimum number or to be composed entirely of non-executive directors. The purpose of the nominations committees in U.S. is to ensure that the board of directors is properly constituted to meets its fiduciary obligations to shareholders and the company. To carry out this purpose, the nominations committee shall.
• Assist the board by identifying prospective director nominees and to select / recommend to the board the director nominees for the next annual meeting of shareholders.
• Oversee the evaluation of the board and management and.
• Recommend to the board, directors nominees for each committee.

Committee Membership and Organization

• The nominations Committee shall be comprised of no fewer than two (2) members.
• The members of the nominations committee shall be independent directors.
• The members of the nominations committee shall be appointed and replaced by the board.

3. Management:

The board of directors and shareholders oversee and monitor the management. This monitoring takes place through oversight of the audit and the company’s accounts which must reflect the true and fair view of the company’s affairs. Directors can inspect these books together with the Registrar and government officials. Shareholders exercise the oversight function by appointing and removing independent auditors through a special resolution at the AGM.

❖ Functions of Management. 29

The functions of the management according to the committee on corporate governance (1999) are.

• Assisting the board in its decision making process in respect of the company’s strategy, policies, code of conduct and performance targets by providing necessary inputs.
• Implementing the policies and code of conduct of the board.
• Managing day to day affairs of the company to maximize shareholder value.
• Providing timely, accurate, substantive and material information to the board, board committees and the shareholders.
• Compliance of all laws and regulations.
• Protecting shareholder’s rights and interests.
• Setting up and implementing effective internal control systems.
• Compliance with code of conduct.
• Co-operating and facilitating efficient working of board committees.

Companies have been victims of serious fraud committed by its executives, sometimes with the knowledge of auditors. The three groups that should exercise control over management are shareholders, auditors and independent directors. Reliance on shareholders to secure management responsibility is inadequate and undependable. They are not assertive and have a vested interest which may conflict with the interest of other stakeholders.

❖ Qualities of Managers
The qualities of managers are as under:

• Strategic awareness and planning.
• Long term vision.
• Commanding respect / leadership.
• Anticipation future trends.
• Individual Responsibility.
• Effective communication skills.
• The share some vision, goals, values, objectives and work on compatible tasks.

Finally, Management role, authority and responsibility depend on the delegation by board.

On above, the important qualities shown senior management.

4. Shareholders:

A shareholder is a member of the company under section 41 of the companies Act, and his name should be entered in the register or members. A person becomes a member by subscribing to memorandum, by allotment, by transfer (purchase in open market) and by transmission (through succession). The facility of nomination (section 109-A) is provided. A person who is competent to contract can become a member. A company may become a member of another company if it is authorized by its memorandum of association. 30
Role of Shareholders.  

Shareholders are owners of the company and enjoy rights and responsibilities. They delegate many of the responsibilities as owners of the company to the Directors who are responsible for corporate strategy and operations. The management team implements the strategy. The basic rights of the shareholders include right to transfer and registration of shares, obtaining relevant information on the company on a timely and regular basis, participating and voting in shareholder meetings electing members of the board and sharing in the residual profits of the company.

The corporate governance framework should protect shareholder’s rights who have a responsibility to make considered use of their voting power. According to SEBZ a company must have appropriate system in place which will enable the shareholders participate effectively and vote in the shareholders meetings. The company should also keep the shareholders informed of rules and voting procedures which govern the general shareholders meeting. The shareholders constituting 1/10 of paid-up capital can also requesting an extraordinary general meeting to consider matters stated for consideration at the meeting. The company law board has also power of a judicial nature to call a meeting on its own motion or on application of a director or member where it has become impractical to hold the meetings.

The board of directors is the proper authority to call for meeting except when the meeting has in the event of default by directors called by requisition by the company Law Board. Notice of the meeting in writing 21 days in advance should be given to every member specifying the place and time of meeting. Unless the articles provide for a larger number of five members personally present is the quorum for a meeting. For the conduct of a meeting the articles of association provide for the appointment of a chairman. The court also has the power to appoint an independent chairman to preside over a meeting where there are factions among shareholders.

The business of the meeting is done in the form of resolution passed at the meeting. Every holder of equity shares except share with differential rights has the right to vote in proportion to his share of the paid-up equity capital of the company. A member is free to distribute his votes. Voting can be done in person, proxy or by postal ballot in respect of business specified. Minutes books containing a fair and correct summary of the proceedings of the meeting are maintained at the registered office of the company for inspection by members, special resolutions, appointment of
managing director, sale of the company’s under taking, borrowing beyond paid-up capital and free-reserves, contributions to charities beyond Rs. 50,000/- or 5% of average net profits, appointment of sole selling agents and voluntary winding-up must be filed with registrar of companies with 30 days.

Money manager with stated long-term investment horizons, etc., in this way, the volatility in trading of its shares and build a stronger shareowner base.

Corporations should encourage short-term “trader” to become long-term “owners”, pointing out the benefits both to the company and to long-term share owners in making its investment decisions in order to fulfill longer term strategies. While investors can and should pursue strategies intended to maximize their rates of return on investment, they should vireo high volatility trading as a risk factor in making their investment decisions.

Empowering Shareholders.

The OECD suggests in a new white paper (The Economist, June 21, 2003) that Asian countries should look for ways to protect minority shareholders that be triggered by shareholders themselves without writing for the courts or regulators to intervene. When shareholders for instance vote unsuccessfully against a large transaction they should have the right to insist that the company buy out their shares at the value prevailing before the transaction took place.  

2.14.2[B] Recommendations Relating to Corporate Governance:

2.14.2. B (1) Recommendations relating to the Board of Directors

(A) Composition and size.

The law should include an enabling provision to prescribe specific categories of companies for which a different minimum number should be laid down.

✓ The new company law should provide for minimum number of directors necessary for various class as of companies. The present requirement is considered adequate.
There need not be any limit to the maximum number directors in a company this should be decided by the company or by its Articles of Association.

Every company should have at least one director resident in India to ensure availability in case of any issue regarding accountability of board.

In order to lay down more responsibilities on companies seeking public subscription, the companies should be required to preserve the composition of the board of directors for two years or till the procured funds are utilized as per the objectives stated in the prospects, whichever is earlier. In case the directors resign from such a company, his liability should continue till the above period.

(B) Selection and Appointment:

Government should not intervene in the process of appointment and removal of directors in non-government companies. The managing/whole-time/executive directors should be in the whole time employment of only one company at any given time.

The committee is in favor of retaining the existing option of the Act (Section 265) regarding adoption of proportionate representation in the board.

Requirement of obtaining central government’s approval under the existing companies Act for non-resident managing director or whole-time director should be done away with.

(C) Tenure:

Both the managing directors as also the whole-time directors should not be appointed for more than 5 years at a time.

(D) Age-limit:

No age-limit need be prescribed in the law. There should be adequate disclosure of age of directors in the company’s documents.

In case of a public company, appointment of directors beyond a prescribed age (say) 70 years should be subject to a special resolution passed by the shareholders.
(E) **Independent Director:**

- Law should recognize the principle of independent directors and spell-out their role, qualifications and liability. Requirement of presence of independent directors should vary depending on the size and type of company. So, number of independent directors may be prescribed through rules for different categories of companies.

- A minimum of one-third of the total strength of the board as independent directors should be adequate, irrespective of whether the chairman is executive or non-executive, independent or not. In the first instance, this requirement should be extended to public listed companies and companies accepting public deposits. The requirements for other types of companies may be considered in due course.

- In certain cases, regulators may specify the number of independent directors required for companies falling within their regulatory domain.

- Nominee directors appointed by a financial institution, banks, or government appointees representing government shareholding should not be deemed to be independent directors as such nominees represent specific interests and cannot, therefore, be termed as independent.

- The expression ‘independent director’ ‘should mean a non-executive director of the company who:

  I. Apart from receiving director’s remuneration does not have, and none of his relatives or firms/companies controlled by him have, any material pecuniary relationship or transaction with the company, its promoters, its directors, senior management or its holding company, subsidiaries and associate companies which may affect independence of the director:

  II. Is not, and none of his relatives is, related to promoters or persons occupying management positions at the board level, or at any one level below the board.

  III. Is not affiliated to any non-profit organization that receives significant funding from the company, its promoters, its directors, senior management or its holding or subsidiary company.

  IV. Has not been, and none of his relatives has been, employee of the company in the immediately preceding year.
V. Is not and none of his relatives is, a partner or part of senior management during the preceding one year, of any of the following:

✓ The statutory audit firm or the internal audit firm that is associated with the company, its holding and subsidiary companies.
✓ The legal firms, and consulting firms that have a material association with the company, its holding and subsidiary companies.

(VI) Is not, and none of his relatives is, a material supplier, service provider or customer or a lesser or lessee of the company.

(VII) Is not, and none of his relatives is, a substantial share holder of the company i.e. owing 2% or more of voting power.

♦ The appointment of independent director should be made by the companies from amongst persons with integrity, possessing relevant expertise and experience and who satisfy the above criteria for independence.

♦ The term ‘material pecuniary relationship’ should be clearly defined for the purpose of determining whether the director is independent or not. It needs to be defined in terms of percentage 10% or more of recipient’s reconsolidated gross revenue/receipts for the preceding year should from a material condition affecting independence. Transaction with an entity in which the directors or his relatives hold more than 2% shareholding should also be considered.

♦ Independent directors / non-executive directors should have the right to;

(a) Call upon the board for due diligence or obtain records for seeking professional opinion by the board;
(b) Inspect records of the company ;
(c) Review legal compliance reports prepared by the company;
(d) In case of disagreement, record their dissent in the minutes.

♦ A non-executive/independent director should be held liable only in respect of any contravention of any provisions of the Act, which had taken place with his knowledge (attributable through board process) and where he has not acted diligently or with his consent or connivance. If the independent director does not initiate any action upon knowledge of any wrong, such director should be held liable. Any follow-up action/dissent of such independent directors, upon
knowledge of any wrong, should be recorded in the minutes of the board meeting.
♦ An independent director should make a self-declaration at the time of appointment and at the time of change in his status that he satisfies the legal conditions for being an independent director.
♦ Board should disclose in the ‘Director’s Report’ that independent directors have given self-declaration and that also in the judgment of the board they are independent. The board should also disclose the basis for determination.

(F) Duties and Responsibilities:

The law should provide only an inclusive and not exhaustive list in view of the fact that no rule of Universal application can be formulated as to the duties of the directors. Certain basic duties should be spelt out in the Act itself, such as;

a) Duty of care and diligence;

b) Exercise of powers in good faith, i.e., discharge of duties in the best interest of the company, no improper use of position and information to gain an advantage for themselves,

c) Duty to have regard in the interest of employees etc.

Punishment for violation of fiduciary duties should be Sufficiently severe so as to deter wrongdoing.

(G) Orientation and Training:

Efforts of various institutions, organizations and associations to train directors should be encouraged in order to enable all companies to access good quality management talent. Such effort should aim at better discharge of fiduciary duties and value enhancing board activities. There should be specific executive development programs aimed at developing the awareness levels of board level appointees. Such persons should also be provided an insight into corporate law compliance requirements.
In the knowledge society they must be update with best practices in corporate governance, current business thinking and statutory requirement. The management institutes can offer part/full time programmers for potential directors.

(H) Number of Directorships and Alternate Directors:

- The total number of directorships any one individual may hold should be limited to a maximum of 15.
- The number of alternate directorships a person holds should fall within the overall limit of directorships.
- An individual should not be appointed as an alternate director for more than one director in the same company.
- An alternate director may be allowed to be appointed for an independent director. Such alternate director should also be an independent director.

(I) Remuneration of Directors:

- Companies should adopt remuneration policies that attract and maintain talented and motivated directors and employees for enhanced performance. Decision on director’s remuneration should be left to the company. However, this should be transparent and based on principles that ensure fairness, reasonableness and accountability.
- There should be a clear relationship between responsibility and performance vis-à-vis remuneration. The policy underlying director’s remuneration should be articulated, disclosed and understood by the investors / stake holders.
- The issue of remuneration and its decision need not be taken by the government on behalf of the company but should be left to its shareholders whose approval should necessarily be taken. Such approval should take into account the recommendations of remuneration committee, through the board.
- What comprises remuneration should be provided for under the rules to the Act. No quantified limit need be prescribed as emphasis should be no disclosures rather than providing limits/ceilings.
✓ These need not be any limit prescribed for sitting fees payable to non-executive directors including independent directors. The company with the approved of shareholders may decide on remuneration in the form of sitting fees and / or profit related commissions payable to such directors for attending board and committee meetings and should disclose it in its “Directors” Remuneration Report forming part of the Annual Report of the company.

✓ In case of inadequacy of profit (or no profit), the company should be allowed to pay remuneration as recommended by remuneration committee through the board and approved by shareholders.

✓ Remuneration received by the directors of the holding company from its subsidiary companies need not be barred but should be disclosed in the Annual Report of the holding company.

✓ The existing method of computation of net profit for the purpose of managerial remuneration, in the manner laid downing sections 349 and 350 of the Act, should be done away with since the current Provisions of the Act adequately ensure that a true and fair picture of the company’s profit is presented.

(J) Disclosure of Directors’ Remuneration and Biographical Information:

✓ All companies should be required to disclose the director’s/managerial remuneration in the ‘Directors Remuneration Report’ and as a part of ‘Directors Report’

✓ The information in the ‘Directors Remuneration Report’ may contain all elements of remuneration package of directors, including severance package and other details like company’s policy on directors’ remuneration for the following year, performance graph etc.

✓ The should be a requirement of disclosure of directors’ back ground, education, training and qualifications, as well as relationship with managers and shareholders.
(K) Board Meetings – Related Matters:

- The requirement of the companies Act, 1956 to hold a board meeting every 3 months and at least 4 meeting in a year should continue. The gap between two board meetings should not exceed four months.

- Notice of every board meeting should be given well in advance (say a period of 7 days) to ensure participation by maximum number of directors.

- Meeting at short notice should be held only to transact emergency business. In such meetings the mandatory presence of at least one independent director should be required in order to ensure that only well considered decisions are taken. If even one independent director is not present in the emergency meeting, then decisions taken in such meeting should be subject to rectification by at least one independent director.

- There should a clean recognition of vital issues for which board discussion in the meeting should be mandatory. These matters should not be left to resolution by circulation. The suggestions made by the companies (Amendment) Bill, 2003 may be taken as the basis.

- Meeting of the board by electronic means (teleconferencing and video conferencing included) should be allowed and directors who participate through electronic means should be counted for attendance and form part of quorum. Minutes should be approved / accepted by such directors who attended by away of teleconferencing and video conferencing by use of digital signature certification. If any director has some reservation about the contents of the minutes, he may raise the issue in succeeding meeting and dissent if any, may be recorded in the minutes of that meeting.

- Failure to attend board meetings for a continuous period of one year should be sufficient ground for vacation of office by the concerned director regardless of leave of absence being given by the board.
(L) Disqualification of Directors:

- The conditions for disqualification of a director should be prescribed by the Act as they relate to the substantive law.
- Directors proposed to be appointed should be required to give a declaration to the board that he is not disqualified to be appointed as a director under provisions of the Act.
- Provision for section 274 (1) (g) of the present Act, prescribing the disqualification of directors should be retained. However, in order to encourage qualified professional to join boards of sick companies it is necessary to amend section 274 (1) (g) of the Act to provide that such disqualification would not be applicable for new directors joining the boards of such companies which have failed to repay their deposits, debentures etc.

(M) Restrictions on Board’s Power:

- The provision of section 293 of the Act should be reviewed. It should be provided that the consent of the shareholders should be obtained through a special resolution for certain items presently mentioned in section 293 (1) (a), (c) and (d) of the Act.
- Shareholders’ approval should be required for sale of whole or substantially whole of the undertaking in that financial year. ‘Whole or substantially whole’ should mean 20% of the total assets of the company.
- Further, certain additional items which should require shareholders’ approval may include sale/transfer of investment in equity shares of other bodies corporate which constitute 20% or more of the total assets of the investing company.

2.14.2. B (2) Board Committees:

(A) Audit committee: 34

* This committee recommends a committee of the board on accounting and financial matters to be termed as the audit committee.
* Majority of the directors of the audit committee should be independent directors if the company is required to appoint independent directors.

* Chairman of the committee should be independent.

* At least one member of the audit committee should have knowledge of financial management or audit or accounts.

* All matters relating to appointment of auditors, examination of the auditor’s report along with financial statements prior to consideration and approval by the board, related party transactions, valuations and other matter involving conflicts of interest should be referred to the board only through the audit committee.

* The recommendation of the audit committee if overruled by the board should be disclosed in the ‘Directors Report’ along with the reasons for overruling.

* The chairman of the audit committee should be required to attend the AGM of the Company to provide clarification on matters relating to audit. If he is unable to attend due to circumstances beyond his control, any other member of the audit committee may be authorized by him to attend the AGM on his behalf.

(B) Remuneration Committee:

* There should be an obligation on the board of a public listed company to constitute a remuneration committee, comprising non-executive directors including at least 1 (One) independent directors.

* The chairman of the committee should be an independent director.

* The remuneration committee will determine the company’s policy as well as specific remuneration packages for its managing/executive directors/senior management.

* The chairman or in his absence at least 1 (One) member of remuneration committee should be present in the general meeting to answer shareholders’ queries.
(C) **Stakeholders’ Relationship Committee:**

* Companies having a combined shareholder/deposit holder/debenture holder base of 1000 or more should be required to constitute a ‘stakeholders’ relationship committee to monitor redressed of their grievances.

* The committee should be chaired by non-executive directors.

2.14. B (3) **Shareholders and stakeholders:**

(A) **Shareholders’ Rights and Shareholders’ voting.**

* The law should indicate in clear terms the rights of members of the company to get all information to which they are entitled in a timely manner. The financial information and disclosure to be provided to shareholders should not be in excessively technical format but should be simple to understand. The information could also be made available through other means like print, electronic media, company website, etc..

* The right of minority shareholders should be protected during meetings of the company. There should be extensive use of postal ballot including electronic media to enable shareholders to participate in meetings.

* A company which has delisted from all the stock exchanges in India and has a shareholder/depositor base of 1000 or more should be mandated to give 1 (one) buyback offer within a period of 3 years of Delisting.

* The provision of section 395 a proposed in the companies (Amendment) Bill 2003 for acquisition of remaining shares (10%) may be considered as a basis for developing an appropriate framework in this regard. The valuation of shares should be done by an independent value to be appointed by the audit committee or the board.

* The board and the management should be protected from undue and unjustified interference from undue and unjustified interference from unscrupulous shareholders acting in the guise of investors’ rights.

* There should be specific provision in the Act to put a limit for entitling shareholders to object a scheme of amalgamation. The limit should be
determined either according to the minimum number of members or as per the minimum percentage of shareholding.

(B) **General Meetings:**

* Every company should be permitted to transact any item of business as it deems fit through postal ballot apart from items for which mandatory postal ballot is prescribed. The government should prescribe a negative list of items which should be transacted only at the AGM and not through postal ballot. The negative items could be the following items of ordinary business.

(I) Consideration of annual accounts and reports of directors and auditors.

(II) Declaration of dividends.

(III) Appointment of directors; and

(IV) Appointment of and fixing the remuneration of the auditors

- Items of business in respect of which Directors/auditors have a right to be heard at the meeting (e.g., in case of a notice for their removal), should not be Transacted through voting by postal ballot.
- AGM may also be held at a place other than the place of its registered office, providing at least 10% members in Number reside at such place (in India only)
- Law should provide for an enabling clause for voting through electronic mode.
- The demand for poll can be made by shareholders holding 1/10th of the total voting power or shares of paid-up value of Rs. 5 lakhs which ever is less. The committee is of the view that the should limit needs to be reviewed to enable conduct of business in an orderly and democratic manner and the same may be prescribed in the rules. Alternatively, possibility of vesting the chairman of the meeting with the power to overrule a demand for poll in certain circumstances may be provided.
- The corporate should be encouraged to seek independent assessment / audit of the conduct of polls during general meetings of the company.
2.14. B (4) Audit and Auditors

Appointment of auditors should be made by the share holders taking into account the recommendations of the board. Which in turn should be arrived at after obtaining the recommendations of the audit committee? In case any of the shareholders wish to propose any other auditor in place of retiring auditors. This process should also necessarily seek the views of audit committee.

* The matter of change of auditors should be left to the shareholders and the auditors themselves rather than to be provided under law.

* Reimbursement of expenses to auditors should not form part of remuneration, but should be disclosed separately in the financial statements along with the auditors’ fees.

* Rendering of all services by the auditors which are not related to audit, accounting records of financial statements, should not be prohibited from being rendered by the auditors subject to a prescribed there should be of materiality.

* All non-audit services may be pre-approved by audit committee.

* An audit firm should, however, be prohibited from rendering the following non-audit services to its audit client and its subsidiaries;

(I) Accounting and book-keeping services relating to accounting records.

(II) Internal audit.

(III) Design and implementation of financial information systems including services related to IT systems for preparing financial or management accounts and information flows of a company.

(IV) Actuarial services.

(V) Investment advisory or investment banking services.

(VI) Rendering of outsourced financial services.
Management functions including provision of temporary staff to audit clients.

The auditor should disclose holdings in the securities of the company, if any, at the time of appointment.

In regard to disqualification of auditors, the amount of indebtedness/guarantee should be increased beyond the present limit of Rs.1000/- and such limit should be prescribed under rules. The indebtedness/guarantee of the auditors should also be extended to cover indebtedness/guarantee to the directors and all entities whose financial statements are required to be consolidated under the Act. The disqualification should be applicable not only to the auditors but also to his relatives, associates, and any entity in which the auditor has a substantial interest.

The work of the auditor should be credible and free from conflict of interests. Therefore, the committee is not in favor of relaxing the prohibition on holding of shares or securities of the company by the auditor. The matter should be examined by the government in consultation with the ICAI in context of the framework of ethical conduct and statutory requirement under the chartered Accountant Act.

Auditors are required to carry out their work with highest standards of excellence and independence. Within the discipline of the legal provisions and the accounting standards. Non-compliance with such standards should invite stringent penalties to be prescribed in the rules.

The basic duties of the auditors and their liability need to be laid down in the law itself.

Government approval for appointment of cost auditor for carrying out cost audit is not considered necessary.

Special audit taken in isolation would serve no useful purpose and hence may be dispensed with.

The law should clearly provide the definition of a government company in context of ownership of the central and / or state government.
* The special exemption and protections to various commercial ventures taken up by government companies in the course of their commercial operations should be done away with so that such entities can operate in the market place on the same terms and conditions as other entities.

* Since statutory audit of a government company is conducted by the statutory auditor appointed by the C & A G in the manner directed by him. The test supplementary audit (by the C & AG officials) is superfluous as it would duplicate audit work already done by statutory auditor. Where any directions are given by the C & AG to the statutory auditor not in accordance with the accounting standard, the auditor may be required to mention the same in the notes on accounts.

2.14. B (5) Internal Control:

* Public listed companies should be required to have a regime of internal financial controls for their own observance Internal controls as mandated by the company with the approval of the audit committee should be certified by the CEO and CFO of the company and in the Directors Report.

2.14.B (6) Financial Reporting:

* The law should provide for an active role for an active role for the shareholders’ associations in ensuring high quality of financial reporting.

* Consolidation of financial statements of subsidiaries with those of holding companies should be mandatory. The current provisions in the Act requiring attaching the accounts of subsidiary companies for circulation to shareholders should be done away with.

* Presentation of consolidated financial statements by the holding company should be in addition to the mandatory presentation of individual financial statements of that holding company.

* The financial statements should be permitted to be sent by electronic means instead of hard copy. In case of listed companies where abridged financial statements are circulated amongst members the full financial
statements should be made available on the web-site and the hard copy there of, should also made available on request.


* A regime of stringent disclosure norms should be provided for incase of companies accessing funds through public offers. There should be adequate and deterrent penalties in law against wrong disclosures.

(A) Disclosure of Directors’ Interest:

The committee recognizes that at par with the international practices in regard to the related party transaction in which the directors or their relatives are interested, a “shareholders approved and disclosure – based regime “should be practiced rather than “Government approval-based regime “in the future Indian context.

* The law should impose a duty on every director to disclose to the company, the contracts or arrangements with the company in which he, directly or indirectly, has any interest or concern.

* The manner, time limits and the extent of such disclosure should be specified in the Act. The notice of relevant disclosure should be made by the interested director to the board at the meeting in which the transaction is to be discussed.

* In adding to the existing requirements [Under section 217 (2AA) the companies Act. 2000] the directors’ ‘Responsibility statement should include that the related party transaction have been entered into at arm’s length and if not, the relationships of the directors in such transactions along with the amounts involved have been disclosed as a part of the ‘Directors Report’ along with management justification thereof.

* Failure to make disclosure should be treated as a default. The concerned directors should be held liable to penalties and he should be deemed to have vacated his office. This should also be a condition of disqualification to hold office of directors of the company for a prescribed period.
* The company should maintain a register in which all such transactions above a prescribed. There’s old value should be entered and register should be kept at the registered office and open to inspection to all members.

(B) **Disclosure of Transactions of the Company with its Holding or subsidiary / Associate companies.**

* Details of such transaction in the ordinary course of business and transacted on an arm’s length basis should be placed periodically before the board through the audit committee, if any.

* Details of transactions not in a normal course of business and / or not on an arm’s length basis should be placed before the board together with management justification for the same. A summary of such transaction with each party should from part of the Annual Report of the company.

* Non-compliance of these provisions should result into :

(I) Penalty on director who authorized such transaction without approval of the board/general meeting.

(II) Transaction being voidable at the option of the board/company.

(III) Director concerned to indemnify the company against wrongful gain made at the cost of the company,

(IV) Director concerned being deemed to have vacated his office.

(V) Disqualification of the director to hold office for a prescribed period.

(C) **Disclosure of Information Relating to Directorship and Shareholdings in the company and in other companies.**

* Every director should disclose to the company.

(I) Personal details as prescribed by rules,

(II) Directorship (including managing directorship, whole time directorship, or manager ship) held by him in any other company/firm,

(III) Shares or debentures held by him as well as his relatives.
(IV) Names of companies in which director either singly or along with his relatives hold not more than a specified percentage of shareholding, to specify by law.

(V) Names of other entities in which he is directly or indirectly interested as partner, member or key person.

(VI) Any changes in respect of above items should be informed to the company within a time specified by law.

2.14.B (8) Key Managerial Personnel:

The committee identifies the following key managerial personnel for all companies.

(I) Chief Executive Officer (CEO) / Managing Director.

(II) Company Secretary. (CS)

(III) Chief Finance officer (CFO)

* Appointment and removal of the key managerial personnel should be by the board of directors.

* The key managerial personnel should be in the whole time employment of only one company at any given time.

2.14. B (9) Officers in Default: 37

* A clear regime for identification of the officers in default is necessary. The liability of such individuals as also other officers of the company in default has to be provided for. In addition to CEOs, CFOs, and CSs, equally important would be the role of qualified professionals such as the accountant, the auditor and lawyer providing corporate advice.

* Such individuals should also be held liable for wrong doing if it can be established that they had not specifically advised against actions or behavior volatile of the law.
In relation to criminal liability of officers in default the rules should provide that:

(I) Director should be liable where they authorized, actively participate in, knowingly permit, or knowingly fail to take active steps to prevent the default;

(II) Managing director / whole time directors / CEO / CFO / CS should be liable on the same conditions, where board has properly charged them with the relevant function,

(III) Any person other than managing director / whole time director / CEO / CFO / CS, who, under the immediate authority of the board / managing director / whole-time director / CEO / CFO / CS, is charged with certain functions including maintenance, filing or distribution of accounts or records should also be liable where he authorized, actively participates in, knowingly permits or knowingly fails to take active steps to prevent the default;

(IV) These definitions should be drafted so as to cover defect to directors, secretaries and managers.

Consideration should be given on a case by case basis to the applicability of offences to receivers, administrators and liquidators.

2.14. B (10) Code of Conduct:

* The committee recognized that there is space for Corporate governance codes to supplements and strengthen the legal provisions. There should be an interactive dialogue between professional bodies and corporate sectors to enable evolution of such codes.

* The codes of conduct for the directors should be developed and disseminated by public sector and professional organizations. Such code should detail the minimum procedure and care that make-up due diligence and care. The presence of such codes would serve to educate both directors and investing public.
2.14. B (11) Protection to whistle Blowers:

* Law should recognize the “Whistle Blower Concept“ by enabling protection to individuals who expose offences by companies, particularly those involving fraud. Such protection should extent to normal terms and conditions of service and from harassment.

2.14. B (12) Small companies:

* The committee recommends a single corporate law framework for application to all companies’ e.g. small companies could be recognized through a scheme of exemptions.

* Company law should enable simplified decision making procedures by reliving such companies from select statutory internal administrative procedures. Such companies should be subjected to reduced financial reporting and audit. Requirements and simplified capital maintenance regimes at a law cost. Such a frame work may be applied to small companies through exemptions, consolidated in the form of a schedule to the Act.

* A definition of small companies may be considered for enabling such a regime. In committee’s view, size may be assessed on the basis of gross assets comprising of fixed assets, current assets and investments not exceeding a particular limit as also turnover. Since the definition of “Small” may change over time, this may be done through rules.

* To qualify for exemption, a small company should neither be a holding nor should a subsidiary of any other company, Associations, charitable companies etc. licensed U/S 25 of the Act not be treated as small companies irrespective of their gross assets.

* Small companies may be exempted from establishing remuneration committee.

* Small companies may be given an option to dispense with the requirement of holding an AGM. Such companies may be permitted to pass resolutions by circulation.
* Special exemptions may be provided for small companies from appointing such personnel (as CEO /Managing director, CFO, CS) on whole time basis. They may obtain services to be considered mandatory under law from qualified professional in practice.

* Relaxation to small companies with regard to the format of accounts to be prescribed in the Act / rules may be considered. If necessary a separate format for small companies may be devised.

* Exemptions from certain disclosure may be considered and relaxations in respect of compliance with accounting standards may be provided for, while notifying the accounting standards. If necessary, a separate accounting standard may be framed for small companies.

2.14. B (13) Investor Education and Protection:

* There is a need for regulators to monitor the end use of funds collected from the public. This should be the responsibility of the share holders of the company who should charge company management with the responsibility coupled with adequate authority to ensure prudent and proper use of funds collected from the public.

* Credit rating would be a good evaluation mechanism and its wide use would b generally beneficial. However, there is no need to mandate credit rating by law except for companies accepting public deposits.

* The companies accepting public deposits should be required to:

(I) Appoint independent directors.

(II) Appoint audit/remuneration/ stakeholders’ relationship committees.

(III) Under take deposit insurance.

(IV) Create adequate case reserve being set aside for repayment of deposits as may be prescribed by the rules.

(V) Undertake credit rating.
(VI) Be subjected to close monitoring in respect of implementation of any scheme for payment of deposits that may be sanctioned by CLB / Tribunal court;

(VI) Be subjected to a stringent disclosure regime, and

(VII) Be subjected to a stringent penalties for irresponsible / fraudulent behavior by the companies.

* The committee feels that compensation to investors may be payable only in cases of established fraud, through a judicial process from the assets of the company or by lifting the corporate veil, those of the promoters or other beneficiaries of such fraud, accessed through a process of disbarment.

* Since share and securities are also legally deemed to be goods under the consumer protection Act 1986. Investors’ should have the option to approach consumer courts as a forum to redress their complaints.

* A timely and simplify institutional structure for dispute resolution is desirable so that investors are not compelled to resort to costly legal proceeding for protection of their rights. In this context the institution of ombudsman for capital market set-up by SEBI should be strengthened.

* There is a need to review the existing provisions of section 205 c of the Act an payment of unpaid dividend to the legitimate claimants, irrespective of the laps of time as the committee feels that law should enable to investor to claim returns on the securities as long as such instruments are held by them.

* There should be a proper regime of disclosure in the public domain so that various agencies are able to reach their conclusion in a non-intrusive manner.

* The law should ensure a disclosure regime that compels companies to disclose material information on a continuous, timely and equitable basis. Use of modern technology, internet, and computers should be enabled to enhance the efficiency of disclosure process.
* The committee perceives a positive role for investors’ Association / NGOs in regard to investors’ education which should be supported by both the government as well as corporate entities.

* There should be a regime of stringent penalties, both civil and criminal, for default in disclosure.
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