“Corporates in the very citadel of capitalism, the United States of America, were mired in problems and were going through a grave crisis of credibility during the very early years of the new millennium. Companies that were held out till then as role models in corporate governance were being threatened with widespread exposures of accounting irregularities and fraudulent practices. The Securities and Exchange Commissions (SEC) set up under the new deal to combat the great depression, appeared to be inadequately equipped to deal with gigantic business organizations such as Xerox, WorldCom and Enron that committed deliberate frauds with a view to boosting their sales revenues and for showing highly inflated profits. If company managements want the market value of their equity shares to climb new peaks year after year, the temptation to fudge accounts and thereby take credit of unearned profits seem to be difficult to resist. Investors, on their part, can neither equate high profits shown by their companies as a sure index of corporate efficiency nor treat a company’s failure to maintain a consistent high profit a failure of corporate governance.”

“WorldCom improperly booked huge expenses in billions, thus inflating profits. Energy firm and Enron, created outside partnerships that helped hide its poor financial condition. Executives earned millions of dollars selling company stocks. The company had to go bankruptcy court. The accounting firm Anderson, was accused of shredding

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1 A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-4
Enron documents and was convicted for obstruction of justice. Energy company, Dynegy, was under investigation for accounting and trading malpractices, in part related to California power crisis. Securities and exchange commissions sued executives of garbage company waste managements for massive accounting fraud resulting in seventeen billions of earnings. The federal administrations of president Bush was quick to slap punitive measures on erring corporations and initiated preventive steps to avoid corporate frauds in future. The Sarbanes-Oxley Act made it mandatory for senior executives to certify reports under oath with the pain of severe penalties if proved wrong. In India, the governance of most of the country’s industrial and business organizations throve on unethical practices at the market place and showed scant regard for the time-less human and organizational values while dealing with their share holders, employees and other stake holders.

**CORPORATE MISGOVERNANCE IN INDIA**

“Organizations in private sector ,barring a few ,indulged in all possible unethical practices to fleece their customers on the one hand and denied the state its due on the other . In India one could see a large number of privately owned business organizations too indulging in corporate misgovernance. The differences that while in state-owned organizations employees at all levels are seen to indulge in, or contribute to, corporate misgovernance, in privately owned business organizations only employees at top levels are seen to be indulging in corporate misgovernance, indicating that in privately owned

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2 A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-4
business organizations employees of the lower levels of the corporation are better controlled.”³

SERIES OF SCAMS THAT SHOOK THE CONFIDENCE OF THE INVESTORS

“The need for corporate governance was first realized in the country with “big bull”, Harshad Mehta’s securities scam that was uncovered in April 1992 involving a large number of banks and resulting in the stock market nose-diving for the first time since the advent of reforms in 1991. Another scam occurred in 1995-1996. Plantation companies Scam saw rupees 50,000 crores from investors who believed plantation schemes would yield huge returns. The so-called non-banking finance companies Scam that occurred in 1995-1997 saw more than rupees 50,000 crores mopped up from the public promising them high returns but vanished. The mutual fund scam saw public sector banks raising between 1995-1998 nearly 15,000 crores by promising huge fixed returns but all of them flopped. Yet another scandal was the one in which BPL, Sterlite and Videocon price ragging happened with the help of Harshad Mehta. The Information Technology scam between 1999-2000 saw firms change their names to include “InfoTech”, and investors saw their stocks run away overnight. The year 2001 witnessed yet another scam in which Ketan Parekh resorted to price rigging in association with a bear cartel”⁴

³ A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-5
⁴ A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-6
ILLEGAL TACTICS OF INDIAN CORPORATES

“Various illegal tactics used by corporates in India over the years are as follows:

- Cornering of industrial licences mainly with a view to pre-empting competitors to enter into their well-entrenched industry
- Using import licences to make a quick profit in the market.
- Illegally holding money abroad to meet business expenses and investments for which government would not allow enough funds.
- Trying to gain special advantages for the business through bribery of concerned officials, generating unaccounted money in the business so as to compensate for penal levels of taxations other “business” expenses and political donations.”

REASONS FOR CORPORATE MISGOVERNANCE

The reasons for corporate misgovernance in India are many. A closed economy, a sheltered, limited need and access to global business, lack of competitive spirit and an inefficient regulatory framework were responsible for the poor governance in India for over forty years, between 1951 and 1991.

INCREASING AWARENESS

“In the after-math of economic liberalization, corporate heavy weights have started mulling over the buzz phrase of corporate governance in conferences. Apart from the Department of company affairs and the institute of company secretaries and trade

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5 A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-6
associations such as the CII and FICCI, (Federation of Indian Chamber of Commerce and Industry capital market regulator, SEBI and companies such as ICICI took the lead in discussing it and recommending its implementation. By April 2003 every listed company adopted the SEBI code of corporate governance.6 Thus the need for good corporate governance is being appreciated as a sound business strategy, and as an important facilitator to tap domestic as well as international capital.

CORPORATE GOVERNANCE IN GLOBAL SCENARIO

Governance in relation to a business organization concerns with the intrinsic, nature, purposes, integrity and identity of the organization and focuses primarily on the relevance, continuity and fiduciary aspects of the organization. It involves monitoring and overseeing Strategic direction, socio-economic and cultural context, externalities of the organization.

Hence Corporate Governance may be called an umbrella term encompassing specific issues arising from interactions among senior management personnel, shareholders, board of directors and the society at large. It deals with the exercise of power over the direction of enterprise, the supervision of executive action, acceptance of a duty to be accountable and regulation of the affairs of the corporation.

With the enactment of Joint Stock Companies Act in 1844, the English Company Law became one of the most permissive in the world and the concept in subsequent years became the basis of corporate Governance and framework for company Law in many jurisdictions including India, Hong Kong, New Zealand, Singapore, South

6 A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-8
Africa, Australia and provinces in Canada. Company Law Developments in the United States, though not directly influenced by the English model, evolved along similar lines reflecting similar ideological traditions.

However development in continental Europe followed a different path. The regulation of corporate entities in Germany adopted for more prescriptive and tight control modes.

In many European countries, shareholders exercise lesser control than the workers in Germany, the representatives of Union serve on supervisory boards. Until recently in Japan shareholder virtually played no role except to provide capital.

In other developing countries like Malaysia and Sri Lanka the need for the better corporate Government has been realized in the wake of liberalization process and privatization of State owned enterprises.

CORPORATE GOVERNANCE MODELS – FROM THE ACADEMIC POINT OF VIEW

A Mckinsey & Company Report published in 2001 under the title Giving New Life to the Corporate Governance Reform Agenda for Emerging Markets suggests that by using a two – version “governance” chain model, we can illustrate the governance practices throughout the world.

MODEL 1

In the first version of Mckinsey’s model called “The Market Model” governance chain, there are efficient, well – developed equity markets and dispersed ownership, something common in the developed industrial nations such as the US, the UK, Canada and Australia. Corporate governance is basically how companies deal fairly with
problems that arise from “separation of ownership and effective control”. This model illustrates conditions and governance practices that are better understood and appreciated and as such highly valued by sophisticated global investors.

MODEL 2

In the second version of Mckinsey’s model called “The Control Model”, governance chain is represented by underdeveloped equity markets, concentrated (family)ownership, less shareholder transparency and inadequate protection of minority and foreign shareholders, a paradigm more familiar in Asia, Latin America and some east European nations. In such transitional and developing economies there is a need to build nature and grow supporting institutions such as a strong and efficient capital market regulator and judiciary to enforce contracts or protect property rights.

CORPORATE GOVERNANCE OF DEVELOPED VERSUS DEVELOPING COUNTRIES

The concept of corporate governance can also be viewed from the context of economic development achieved by countries. The Anglo – American, German, Japanese and other mature and developed economics have all well functioning market system and highly developed legal institutions, although there are considerable differences between them as there are in various types of democracy.

In the context of developed societies, the essence of corporate governance as expressed in the words of Patricia A. Nodoushani and Omid Nodoushani is as follows: “It is a relationship among various participants in determining the direction and
performance of a corporation. However corporate governance goes beyond the simple concept of who is in charge and who has the power. Chief among its goals are improving shareholder value and supporting a continuing commitment to growth.”

The former President of World Bank, J.Wolfensohn, expressed the view that “corporate governance is about promoting corporate fairness, transparency and accountability.”7 According to some other experts: Corporate governance means doing everything better than the quality of outside directors; to encourage people to think of long –term relations; information needs of all stakeholders are met and to ensure that executive management is monitored properly in the interest of shareholders.

Sir Adrian Cadbury, chairman of the Cadbury committee, defined the concept thus: “Corporate governance is defined as holding the balance between economic and social goals and also between individual and communal goals. The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interest of individuals, corporations and society. The incentive to corporations is to achieve their corporate aims and to attract investment. The incentive for states is to strengthen their economics and discourage fraud and mismanagement.”8

7- Financial Times 21st June 1999
Experts at the Organization of Economic Co-operation and Development (OECD) have defined corporate governance as “the system by which business corporations are directed and controlled”. For them, “the corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such, as the Board, managers, shareholders and other stakeholders, and spells out the rules and procedures from making decisions on corporate affairs.”

All these definitions which are shareholder – centric capture some of the most important concerns of governments in particular and the society in general. These are: (i) management accountability, (ii) providing adequate investment to management (iii) disciplining and replacement of bad management, (iv) enhancing corporate performance, (v) transparency, (vi) shareholder activism, (vii) investor protection, (viii) improving access to capital markets, (ix) promoting long – term investment and (x) encouraging innovation.

From the standpoint of developing economies and transition societies, ensuring corporate governance becomes difficult in the absence of well – developed corporate culture, capital market, money, regulatory systems, well – defined and suitable public policies, proactive governments, knowledgeable stakeholders and presence of corruption, bribery, discrimination and a culture of accepting misgovernance, fraud and corporate misdemeanor as part of human frailties.

9- www.oecd.org
Shareholders, on the other hand, have remained scattered, mute and often oblige managements, and pass resolutions without a murmur for the meagre dividends and petty gifts. In such a scenario, developing strong and powerful regulatory institutions, legal structures and evolving healthy precedence is of great importance.

“Corporate governance systems depend upon a set of institutions (laws, regulations, contracts, and norms) that create self – governing firms as the central elements of a competitive market economy. These institutions ensure that the internal corporate governance procedures adopted by firms are enforced and that management is responsible to owners (shareholders) and other stakeholders.

When it is practised under a well-laid out system, it leads to the building of a legal, commercial and institutional framework and demarcate the boundaries within which these functions are performed.”

Narrow versus Broad perceptions of Corporate Governance

“Corporate Governance can also be defined from a very narrow perception to a broad manner. An article that appeared in Financial Times in 1997 holds: “Corporate governance......... is the relationship of a company to its shareholders or, more broadly, as its relationship to society.”

\[\text{Sources: } \text{A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-10-13}\]

1 Financial Times 1999
The earliest definition of corporate governance in its narrow sense is from the Economist and Nobel Laureate, According to Milton Friedman. “Corporate governance is to conduct the business in accordance with the owner’s or shareholders’ desires, which generally will be to make as much money as possible, while conforming to the basic rules of the society embodied in law and local customs”\(^{12}\). This definition is based on the economic concept of market value maximization that underpins shareholder capitalism. In the present day context, Friedman’s definition is narrow in scope. In this narrow sense, corporate governance can be viewed as a set of arrangements internal to the corporation that defines the relationship between the owners and managers of the corporation.

The World Bank defines corporate governance from two different perspectives. From the standpoint of a corporation, the emphasis is placed on the relations between the owners, management, board and other stakeholders (the employees, customers, suppliers, investors and communities). Major significance in corporate governance in this narrow perspective is given to the board of directors and its ability to attain long term, sustained value by balancing these interests. From a public policy perspective, corporate governance refers to providing for the survival, growth and development of the company, and at the same time, its accountability in the exercise of power and control over companies. The role of policy is to discipline companies and, at the same time, to stimulate them to minimize differences between private and social interests. The OECD also offers a broader definition: “..... Corporate governance refers to the private and public institutions, including laws, regulations and accepted business practices, which together govern the relationship in a market economy, between corporate, managers and

\(^{12}\) A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-14
entrepreneurs (corporate insiders) on one hand, and those who invest resources in corporations, on the other.”

**GOVERNANCE IS MORE THAN JUST BOARD PROCESSES**

“Governance is more than just Board processes. It involves the full set of relationship between a company’s management, Its Board, its shareholders and its other stakeholders, such as its employees and the community in which it is located. The quality of governance is directly linked to the policy framework. In the 21st century, stability and prosperity will depend on the strengthening of capital markets and the creation of strong corporate governance systems.”

**REQUIREMENTS OF CORPORATE GOVERNANCE ACCORDING TO OECD**

1. **RIGHTS OF SHAREHOLDERS**

“Shareholders have the right to know the capital structures of their corporation and arrangements that enable certain shareholders to obtain control disproportionate to their holding. All transactions should be transparent prices and under fair conditions. Anti – takeover devices should not be used to shield managements from accountability. Institutional shareholders should consider the costs and benefits of exercising their voting rights.

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13 A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-10-13
14 - www.oecd.org
2. EQUITABLE TREATMENT OF SHAREHOLDERS

The OECD and other organizations such as APEC (Asia-pacific Economic Co-operation) have stressed the point that all shareholders including minority and foreign shareholders should get equitable treatment. All shareholders should have equal opportunity for redressal of their grievances and violation of their rights. Shareholders should not face undue difficulties in exercising their voting rights. Any change in their voting rights should be subject to a vote by shareholders. Insider trading and abusive self-dealing that are repugnant to the principle of equitable treatment of shareholders should be prohibited. Directors should disclose any material interests regarding transactions. They should avoid situations involving conflict of interest while making decisions. Interested directors should not participate in deliberations on decisions that concern them.

3. ROLE OF STAKEHOLDERS IN CORPORATE GOVERNANCE

Apart from dealers, consumers and the government who constitute the stakeholders’ group, there are others who ought to constitute. Banks, bondholders and workers, for example are important stakeholders in the way in which companies perform and make decisions. Corporate governance framework should, apart from recognizing the rights of shareholder, allow employee representation on board of directors, profit sharing, and creditors’ involvement in insolvency proceedings etc. For active stakeholder participation, it should be ensured that they have access to relevant information.
4. DISCLOSURE AND TRANSPARENCY

The OECD lays down a number of provisions for the disclosure and dissemination of key information about the company to all those entitled for such information. These may range from company objective to financial details, operating results, governance structure and policies, the Board of Directors, their remuneration, significant foreseeable risk factors and material issues regarding employees and other stakeholders.

5. RESPONSIBILITIES OF THE BOARD

The OECD guidelines explain in detail the functions of the Board in protecting the company, its shareholders and its other stakeholders. These functions would include concerns about corporate strategy, risk, executive compensation and performance, accounting and reporting systems, monitoring effectiveness and changing them, if needed. “15

A HISTORICAL PERSPECTIVE OF CORPORATE GOVERNANCE FROM A NARROW TO A BROAD VISION

“With the passage of time, it is now accepted that firms should respond to the expectations of large categories of stakeholders which include employees, consumers, institutional investors, government and the society as a whole. These diverse interests are to be harmonized and accommodated. Firms can achieve long-run value maximization only if they respond to the expectations of these increasingly large number of stakeholders. Externalities such as product safety, job safety, and environmental impacts

15 A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-17
have increased the importance and significance of better governance of corporations to achieve these ends in recent years. Still further additions to the wide range of corporate governance practices include as indicated earlier business ethics, social responsibility, management discipline, corporate strategy, life-cycle development, stakeholder participation in the decision making processes, and promotion of sustainable economic development.

THE GROWTH OF MODERN IDEAS OF CORPORATE GOVERNANCE FROM THE USA

The seeds of modern ideas of corporate governance were probably sown by the Watergate scandal during the Nixon presidency in the US. Subsequent investigations on the scandal revealed that the regulators and legislative bodies failed to control and stop several major corporations from making illegal political contributions and bribing government officials. The need to arrest such unhealthy trend was translated into the legislation of the Foreign and Corrupt Practices Act of 1977 in America that provides for the maintenance and review of systems of internal control in an establishment. In the same year, the Securities and Exchange Commission (SEC) proposed mandatory reporting on internal financial controls.

CORPORATE SCAMS IN UK

A series of corporate scams and collapses in that country occurred in the late 1980 and early 1990s which worried banks and investors about their investments and led the
government in the UK to realize the inefficacy of the then existing legislation and self-regulation. Illustrious business enterprises, which witnessed spectacular growth in boom time, became disastrous failures later due to poor management and lack of effective control.

THE CADBURY COMMITTEE

When it was realized in England that the existing rules and regulations were not adequate to curb unlawful and unfair practices of corporates so as to protect the unwary investors, it was thought necessary to look at the issues involved afresh and look for remedial measures. It was with this view a committee under the chairmanship of Sir Adrian Cadbury was appointed by the London Stock Exchange in 1991. Sir Adrian Cadbury was entrusted in 1991, by the London stock Exchange, with the task of drafting a code of practices to assist corporations in defining and applying internal controls to limit their exposure to financial loss in England. The Cadbury committee investigated extensively the accountability of the board of directors to shareholders and to the Society. The committee that submitted its report along with the code of Best practices in December 1992 elaborated the methods of governance needed to achieve a balance between the board and their proper accountability.

THE AFTERMATH OF CADBURY REPORT

After five years of the Cadbury Report, public confidence in corporates in England was again shaken by further scandals. To deal with the situation, a “committee on Corporate Governance” headed by Ron Hampel was constituted with a brief to keep
up the momentum by assessing the impact of Cadbury Report and developing further guidelines. The final report of the Hampel committee submitted in 1998 contained some important and progressive guidelines, especially the extension of directors’ responsibilities to “all relevant control objectives including business risk assessment and minimizing the risk of fraud”.16

CORPORATE GOVERNANCE IN THE BANKING SECTOR

Some bank failures in the West underlined the necessity of close monitoring of the banking system. Weakness in the banking system of a country can threaten the financial stability, both within the country and within globally. The Basel Committee on Banking supervision has been working in this field for many years, both directly and through its many contacts with banking supervisors in every part of the world.

Both the government and the Reserve Bank of India need to bring about significant changes in the corporate governance mechanism adopted by banks. As a matter of principle, Reserve Bank of India should not appoint its nominee on the boards of bank to avoid conflict of interests. Presently the shareholders are denied the basic right of approving annual accounts and dividends. Strong corporate governance in banks needs greater transparency and disclosures besides committees for nomination of boards, for remuneration and for stakeholder. The audit committees of the banks are also required to go for deep checks for both internal and external auditors. Since banks are highly leveraged entities, their failures will pose large risks to entire economic system, so their corporate governance mechanism should relatively be much tighter.

16 A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-20-21
ISSUES IN CORPORATE GOVERNANCE

1. DISTINGUISHING THE ROLES OF BOARD AND MANagements

Constitutions of more and more companies stress and underline that the business is to be managed “by or under the direction of” the board. In such a practice, the responsibility for managing the business is delegated by the board to the CEO, who in turn delegates the responsibility to other senior executives. Thus the board occupies a key position between the shareholders (owners) and the company’s management (day-to-day managers of the company’s resources). As per this arrangement, the board of a listed company has the following functions

(a) To select, decide the remuneration and evaluate on a regular basis, and when necessary, change the CEO.

(b) To oversee (not directly, but indirectly) the conduct of the company’s business to evaluate whether or not it is being correctly managed.

(c) To review and, where necessary, approve the company’s financial objectives and major corporate plans and objectives.

(d) To render advice and counsel to top management.

(e) To identify and recommend candidates to shareholders for electing them to the board of directors.

(f) To review the adequacy of systems to comply with all applicable laws and regulations and

(g) To carry out all other functions required by law to be performed.
2. COMPOSITION OF THE BOARD AND RELATED ISSUES

A board of directors is a committee elected by the shareholders of a limited company to be responsible for the policy of the company. Sometimes, full-time functional directors are appointed, each being responsible for some particular branch of the firm’s work. The composition of board directors refers to the number of directors of different kinds that participate in the work of the board. Over a period of time there has been a change as to the number and proportion of different types of directors in the board of a limited company.

“The SEBI – appointed Kumar Mangalam Birla Committee’s Report defined the composition of the Board thus: “The Board of Directors of a company shall have an optimum combination of executive and non – executive directors with not less than 50per cent of the board of directors to be non-executive directors. The number of independent directors would depend whether the chairman is executive or non-executive. In case of a non-executive chairman, at least one –third of the board should comprise independent directors and in case of executive chairman, at least half of the board should be independent directors”17

3. SEPARATION OF THE ROLES OF THE CEO AND CHAIRPERSON

“The composition of the board is a major issue in corporate governance as the board acts as a link between the shareholders and the management and its decisions affect the performance of the company.

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It is now increasingly being realized that the practice of combining the role of the chairperson with that of the CEO as is done in countries like the US and India leads to conflicts in decision making and too much concentration of power in one person resulting in unsavoury consequences. In the United kingdom and Australia, the CEO is prohibited from being the chairperson of the company. The role of the CEO is to lead the senior management team in managing the enterprise, while the role of the chairperson is to lead the board, one important responsibility of the Board being to evaluate the performance of senior executives including the CEO. Combining the role of both the CEO and chairperson removes an important check on senior management’s activities” 18

4. COMMITTEES ON THE BOARD

Many Committees on corporate governance have recommended in one voice the appointment of special committees for (i) nomination, (ii) remuneration and for (iii) auditing. These committees would lessen the burden of the board and enhance its effectiveness professional expertise in their chosen fields and long years of work experience would help the respective committees decide issues objectively and in a manner that would promote the long term interests of the organisation.

5. APPOINTMENTS TO THE BOARD AND DIRECTOR’S RE-ELECTION

The board or its specially constituted committee selects and appoints the prospective director and gets the person formally “elected” by the shareholders at the ensuing Annual General Body meeting.

18 IFSA Guidelines – Investment and Financial Services Associations (1999), Corporate Governance: A guide for investments and corporations
Shareholders in fact only endorse the board’s nominees and it is only in rarest of rare cases the shareholders refuse to ratify the board’s nominees for directorship. There are other issues of corporate governance in relation to the Board’s appointments such as appointment of a nomination committee, terms of office, duties, remuneration and re-election of directors and composition of the board on which several committees have made their own recommendations.

6. DIRECTORS AND EXECUTIVES’ REMUNERATION

According to the Cadbury Report: “The over-riding principle in respect of Board remuneration is that shareholders are entitled to a full and clear statement of Directors’ present and future benefits, and how they have been determined.” Other committees on corporate governance have also laid emphasis on other related issues such as pay-for-performance, heavy severance payments, pension for Non-executive directors, appointment of remuneration committee and so on.

7. DISCLOSURE AND AUDIT

The Cadbury Report termed the annual audit as one of the cornerstones of corporate governance. Audit also provides a basis for reassurance for everyone who has a financial stake in the company. There are several issues and questions relating to auditing which have an impact on corporate governance. There are, for instance, questions such as: (1) Should boards establish an audit committee? (ii) if yes, how should it be composed? (iii) How to ensure the independence of the auditor? (iv) what are the precautions to be taken or what are the positions of the auditors? (v) should individual

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directors have access to independent resource? and (vi) should boards formalise performance standards?

8. PROTECTION OF SHAREHOLDER RIGHTS AND THEIR EXPECTATIONS

This is an important governance issue which has considerable impact on the rights and expectations of shareholders. Corporate practices and policies vary from country to country. There are a number of question relating to this issue such as: (i) Should companies always adhere to one–share-one vote principle? (ii) should companies retain voting by a show of hands or by poll? (iii) Can shareholder’s resolution be bundled? i.e. to place together before shareholders for approval a resolution that contains more than one discrete issue and (iv) should shareholder approval be required for all major transactions?

9. DIALOGUE WITH INSTITUTIONAL SHAREHOLDERS

The Cadbury Committee recommends that institution investors should maintain regular and systematic contact with companies, apart from their participation in general meeting of shareholders, use their voting rights positively, take a positive interest in the composition of the board of directs of companies in which they invest, and above, all recognize their rights and responsibilities as “owners” who should act in the best interests of those whose money they have invested by influencing the standards of corporate governance and by bringing about change in companies when necessary, rather than by selling their share, and quitting the companies.
If institutional investors have to exercise their rights and carry out their responsibilities, companies have to provide them the required information and facilities.

10. THE SAY OF INVESTORS IN MAKING A COMPANY “SOCIALLY RESPONSIBLE CORPORATE CITIZEN”.

The institutional investors should act in the best financial interests of the beneficiaries. This is based on the assumption that socially responsible behavior of corporations such as ecological preservation, anti-pollution measures and producing quality and environment-friendly products which always enhance costs and thus reduce profits. On the other hand, they benefit corporations in the long run and cite the examples of Ford Motors, Johnson & Johnson etc., to prove the point.

INVESTORS’ PREFERENCE FOR GOOD GOVERNANCE

BENEFITS TO SOCIETY

According to John D. Sullivan, Corporate Governance brings to the society innumerable benefits. These benefits are as follows:

- “A strong and vibrant system of corporate governance can be a major benefit to society. Even in developing countries where shares of most firms are not actively traded on stock markets, adopting standards for transparency in dealing with investors and creditors will bring benefit to all and also it helps to prevent systematic banking crises. Research has proved that countries with stronger corporate governance protections for minority shareholders have much larger and more liquid capital markets."
• In many societies combating corruption is not a subject that is easy to deal with both because of political sensitivities and potential legal action. When companies try to be transparent, have systems that provide full disclosure of accounting and auditing procedures, allow transparency in all business transactions, corruption will not have a big role to play.

• Better corporate governance procedures can also improve the management of the firm and help a great deal in working out business strategy. It needs to be stressed that good corporate governance system also has to include improvements in management system. \(^{20}\)

**BENEFITS OF GOOD CORPORATE GOVERNANCE TO A CORPORATION**

**1. CREATION AND ENHANCEMENT OF A CORPORATION’S COMPETITIVE ADVANTAGE**

“Competitive advantage grows naturally when a corporation or its services facilitate the creation of value for its buyers. Corporations which develop their strategies by involving all levels of employees create widespread commitment to make the strategies succeed. Practical examples of strategies that create value to corporations are sales and marketing strategies, customers base and branding strategies.

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\(^{20}\) Sullivan, John D, Building sound Corporate Governance for Global Competitiveness, Centre for International Pvt. Enterprises, www.cipe.org
2. ENABLING A CORPORATION PERFORM EFFICIENTLY BY PREVENTING FRAUD AND MALPRACTICES

The code of Best Conduct-policies and procedures that govern the behaviour of individuals of a corporation-form part of corporate governance. This enables a corporation to compete more efficiently in the business environment and prevents fraud and malpractices that destroy business from inside. Failure in management of best practice within a corporation has led to crises in many instances.

3. PROVIDING PROTECTION TO SHAREHOLDERS’ INTEREST

Corporate governance is a set of rules that focuses on transparency of information and management accountability. It imposes fiduciary duty on management to act in the best interests of all shareholders and properly disclose operations of the corporation. This is particularly important when ownership and management of an enterprise are in different hands as these are in corporates.

4. ENHANCING THE VALUATION OF AN ENTERPRISE

Improved management accountability and operational transparency fulfil investors’ expectations and confidence on management and corporations, and in return increase the value of corporations.

5. ENSURING COMPLIANCE OF LAWS AND REGULATIONS

With the development of capital markets and the increasing investment by institutional shareholders, and individuals in corporations that are not controlled by
particular shareholders, jurisdictions around the world have been developing comprehensive regulatory frameworks to protect investors. Corporate governance ensures the long – term survival of a corporation and thereby enables its shareholders long-term benefits.\textsuperscript{21}

CONCLUSION

Corporate governance ensures transparency, full disclosures and accountability of companies to all its stakeholders. The latest revised OECD principles place their thrust on six major areas of corporate governance. (i) They call upon governments to put in place an effective institutional and legal framework to support good corporate governance practices; (ii) they call for a corporate governance framework that protects and facilitates the exercise of shareholders’ rights; (iii) they strongly support equitable treatment of all shareholders including minority and foreign shareholders; (iv) they recognize the importance of the role of stakeholders in corporate governance; (v) they stress the importance of timely, accurate and transparent disclosure mechanisms and finally (vi) they deal with Board structures, responsibilities and procedures. All issues of corporate governance, of course, emanate from and centre around these six major areas.

CORPORATE GOVERNANCE IN GLOBAL SCENARIO

Corporate Governance practices diverge between different jurisdictions, based on board structures, legal frameworks, interpretations of the ‘Corporate’ concept, prevalence of competition, Role of courts and other factor, which vary according to their evolution in specific cultures and countries.

\textsuperscript{21} A.C. Fernando, Corporate Governance, Principles policies and practices, Pearson Education, India 2006, p-28-29
If we consider international corporate Governance as comprising these dissimilar practices as worker co-determination obtaining in continental Europe, two tier board structures in Germany, the family domination of listed companies of overseas Chinese groups etc. it would seem courageous even to speak of international practices.

With the enactment of Joint stock companies Act in 1844, the English company laws became one of the most permissive in the world and the concept in subsequent years became the basis of corporate governance and framework for company law in many jurisdictions including India, Hong Kong, New Zealand, Singapore, South Africa, Australia and provinces in Canada.

However development in continental Europe followed a different path. In many European countries, shareholders exercise lesser control than the workers and similarly, in Germany, the representations of union serve on supervisory boards. Shareholders virtually played no role except to provide capital.
1. COMMITTEES ON CORPORATE GOVERNANCE: GLOBAL PERSPECTIVE

A number of Committees were set-up to look into the various aspects of corporate governance. These include:

- Mervyn E. Kings Committee on Corporate Governance (1994).
- Business Round Table (BRT) Statement on Corporate Governance (1997).
- Hampel Committee on Corporate Governance (1998).
- Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees (1999).
- OECD Principles of Corporate Governance (1999) and
- CACG principles for Corporate Governance in Commonwealth (1999).

These committees / codes recommended the following in relation to accounts, reporting audit.
❖ CADBURY COMMITTEE ON FINANCIAL ASPECTS OF CORPORATE GOVERNANCE (1992)

- The Audit committee must have minimum three members, written terms of reference and authority to investigate.
- Listed companies must publish full financial statements annually and half yearly reports interim.

❖ CODE OF BEST PRACTICE INCORPORATE

- Board must present assessment of company’s position.
- Directors must report on effectiveness of internal control systems and
- Aspects must be included by audit committee.

❖ KING’S COMMITTEE ON CORPORATE GOVERNANCE (1994)

- Effective internal Audit function.
- Establishment of Audit Committee.
- Observance of highest level of business and professional ethics and
- Accounting standards in line with international standards.
• Members of Audit Committee must be independent.
• Audit Committee must consist of independent directors only.
• Audit committee must have minimum of three directors each to be financially literate.
• Audit committee must have formal written charter, approved by the full board, specifying responsibilities, and structure, process and membership.
• Charter must specify outside auditors responsibility towards board and committee.
• Companies must attach with Annual Report a letter from Audit Committee as to whether or not:
  ➢ Management reviewed the audited financial statements with the committee;
  ➢ Outside auditors discussed with the committee, their judgement; and
  ➢ Committee believes that company’s financial statements are fairly presented in conformity with Generally Accepted Accounting Practices (GAAP).
CACG GUIDELINES PRINCIPLES FOR CORPORATE GOVERNANCE IN THE COMMONWEALTH (1999) COUNTRIES

- Ensure that the corporation complies with all relevant laws, regulations and codes of best business practice;
- Ensure that the corporation communicates with shareholders and other stakeholders effectively;
- Serve the legitimate interests of the Shareholders of the corporation and account to them fully;
- Regularly review process and procedures to ensure the effectiveness of its internal systems and control, so that the decision making capability and the accuracy of its reporting and financial results are maintained at a high level at all times and
- Ensure annually that the corporation will continue as a going concern for its next fiscal year.

HAMPEL COMMITTEE ON AUDIT AND ACCOUNTABILITY
COMPANIES AND AUDITORS SHOULD APPLY THE FOLLOWING PRINCIPLES

- Financial reporting – The Board should present a balanced and understandable assessment of the company’s position and prospects.
- Internal Control – The Board should maintain a sound system of internal control to safeguard shareholder’s investments and repay assets.
• Relationship with auditors – The Board should establish forms and transparent arrangements for maintaining and appropriate relationships with the company’s auditors. Audit committee should be established and be responsible to board. It should review the scope and result of the audit, its cost effectiveness and the independence and objectivity of auditors.

• External Auditors – The external auditors should independently report to shareholder in accordance with statutory and professional requirements and independently assure the board on the discharge of its responsibilities (financial reporting, internal control) in accordance with professional guidance.

• The auditors have a dual responsibility – The public report to shareholders on the statutory financial statements and on other matter and additional private reporting to directors on operational matters.

CORPORATE GOVERNANCE PRACTICES IN SOME COUNTRIES

The guidelines and principles of Corporate Governance, no doubt, vary according to the corporate environment prevailing in respective regions and countries. But on the others hand every country endeavours that the Joint Stock Companies that operate these do flourish and grow in a manner to provide employment, wealth and satisfaction and to uplift the standard of living and also enhance social cohesion. This is possible when business entities are competitive, efficient transparent and fair in the liberalized, private and globalized business environment.
The current emphasis on corporate governance owes its origin to a number of factors. The 20th Century witnessed significant changes in our economic environment. There has been an unprecedented expansion in international trade and investment. Multinational corporations today command enormous financial and non-financial resources, have distinct global presence, enjoy a great deal of economic and political clout.

The corporate form of organisation has already emerged as the predominant form of business organisation. Breathtaking strides in the area of infotech remarkable innovations in the area of financial instruments integrate national economics into a global framework. The focus throughout much of the world is on liberalization and globalization. Companies have to respond to their opportunity and threat perceptions in today’s environment with the least possible delay. Capital markets, local and global, can be tapped for more easily by companies that perform satisfactorily. They, therefore, have to be well governed.

The way corporations are run is of vital importance not merely to the shareholders of such corporations, but to all other stakeholders and even to the polity of our world today. The debt crisis in some Latin American Countries some year ago and the recent financial problems in South-East Asia, are ample reasons for seeking good governance. In our economically integrated world the ripple effects can hurt anyone. There is a need for standardization of accounting
procedures and disclosure norms and it takes into account the legal and institutional framework in various countries of the world.

CORPORATE GOVERNANCE IN THE UNITED KINGDOM AND THE UNITED STATES OF AMERICA

In the UK and the USA the corporate system and structure is characterized by diffused ownership and shareholding, as a large percentage of the shares is subscribed to by the public. They have a well developed capital market with active shareholders participation. Firms are subject to strict disclosure norms and investor protection. The focus of good governance in these countries is the code of the best practice. The focus on issue of corporate governance culminated in the Cadbury Report on the financial aspects of Corporate Governance in 1992, the Greenbury Report on Director’s remuneration in 1995, the preliminary and final Hampel Reports on corporate governance in 1997 and 1998.

THE UNITED KINGDOM

The United Kingdom has ruled the world and English continues to be the most widely spoken language. Their influence has been tremendous in all walks of life. The theme of Corporate Governance has been very close to the heart of Accounting and corporate profession in the U.K. Cadbury committee was set-up by the Financial Reporting Council, London, Stock Exchange and the accountancy profession in May 1991
vod BOARD OF DIRECTORS

• Meeting of Board of Directors should be regularly held.

• It must retain full and effective control over the company.

• It must monitor the executive development.

• No one individual be given unfettered power. A balance be maintained between power and authority.

• Non-executive directors having sufficient calibre and the number of the directors be included in the board of directors.

• Direction and control of the company should be firmly in their hand.

• In dependent professional advice at company’s expense be obtained for furtherance of their duties.

• For getting benefit from the Secretary of the Board and enabling him to stay independent, the following guidelines be followed:
  ➢ Access to advice and service,
  ➢ Procedures are followed and rules and regulations are compiled with and
  ➢ Board as a whole should examine the question of removal of the secretary.

vod NON-EXECUTIVE DIRECTORS

1. The role of non-executives directors may extend to the following:

• Contribute towards independent judgement.

• Areas of contributions may include:
Strategy performance,  
Key appointments, and  
Standards of Conduct  

2. For ensuring fairness and independence, the following guidelines be followed:

• Be independent of management.

• Fees should reflect the time which they commit to the company.

• They should be appointed for specified terms and reappointment should not be automatic.

• They should be selected through a formal process.

Board as a whole should take this decision.

❖ EXECUTIVE DIRECTORS

• The term of service should not exceed three years without the shareholders approval.

• There should be transparent disclosure of directors and chairman’s total emolument, separately together with the highest paid UK directors. Pension contributions and stock operations be separately highlighted. Salary and performance-related elements be separately stated including the basis on which performance is measured.

• A remuneration committee should be set-up to recommend the pay to executive directors. This committee should be made up wholly or mainly of non-executive directors.
**REPORTING AND CONTROLS**

- Board must accept it a duty to present a balanced and understandable assessment of the company’s position.

- An objective and professional / balance should be maintained between Board and the internal and external auditors.

- The Board should set-up an audit committee of at least three non-executive directors. Terms of reference must be in writing and should clearly deal with its authority and duties.

- The directors should report on the effectiveness of the company’s system of internal control. They should also report that the business is a going concern. Supporting assumptions or necessary qualification should also be included. The Corporate Governance issue was examined in the UK. Sir Ronald Hampel, ICI Chairman, was appointed to submit a report by the end of 1997. This task has already been completed.

An excerpt from News Release issued on January 3, 1997 by the Charted Institute of Management Accountants (CIMA) in their evidence to the UK Hampel Committee on corporate Governance is quoted below:

““The Cadbury code on Corporate Governance must be given extra weight by reflecting expected best practice rather than just recommended practice””\(^\text{22}\)

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\(^{22}\) Parmjit Kaur, Globalisation: Corporate Governance and its position in India; Corporate Governance, Deep and Deep publications Pvt. Ltd, New Delhi 2003, P-99-100
CIMA’S SUBMISSION EMPHASIS AREAS

- That all public companies should be expected to have internal audit function (except in the minority of cases where this would be inappropriate owing to the nature of the organisation);
- That the internal audit function’s remit should cover the whole system of controls established by management, not just internal financial controls.
- That public reporting on internal control is of limited value and should focus on the measures in place rather than try to assess their effectiveness; and
- That the benefit of private reporting, i.e., between internal and external auditors, Audit Committees and senior management need to be more positively portrayed and the practice encouraged.

CIMA encouraged the Committee to look at the broad control environment of which the financial aspects of corporate governance form but a part, and in particular, at corporate ethics, codes of conduct and behaviour. Experts from Pat Redrup, FCMA, Vice-Chairman of CIMA’s Law and Parliamentary Committee are as under:

“Most companies have had time to develop their practice and systems to meet the Cadbury code. We are seeking evolutionary changes rather than making revolutionary recommendations. CIMA believes that the Hampel Committee Review should concentrate on taking some aspects of the code further to achieve expected best practice and to also look at the emerging issues of
corporate ethics and conduct within such best practices, Corporate behavioural health checks are becoming just as important as good financial performance”. The Hampel Report was released in January 1998.

**HONG KONG**

The Accountancy Profession of Hong Kong was generally influenced by events occurring in the United Kingdom. The Cadbury Committee Report was read with keen interest and now two reports were developed in Hong Kong by the Hong Kong Society of Accounts. These consisted of the following:


“An exclusive cover story on the then of Corporate Governance was published in the Journal entitled, “The Hong Kong Accountant” released by the Hong Kong society of Accountants in October, 1996. A magnificent step was taken by the above Society by releasing a ten point code for effective Corporate Governance. These include the following:

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23 Parmjit Kaur, Globalisation: Corporate Governance and its position in India; Corporate Governance, Deep and Deep publications Pvt. Ltd, New Delhi 2003, P- 101
• Compliance matter should be identified.
• Same family must not have more than 50% member of Board of Directors.
• There should be Chief Financial Officer (CFO) through a mandatory provision.
• Attendance record of Board at Annual General Meeting should be maintained.
• Four board meetings must be held every year. However, six meetings are preferred.
• Other fees paid to auditors should be separately disclosed.
• There should be separate disclosure regarding Corporate Governance in the annual report of the company.
• An Audit Committee, with defined functions, should be established.
• Interim reports containing balance sheet, income statement and cash flow should be released and
• The above interim reports should be reviewed by auditors.”

MALAYSIA

The inspiring leadership of Dr. Muhammad Mahatair, Prime Minister of Malaysia, has set an exemplary guidance of “Good Government Governance”. This has the snowball effect. Consequently, the theme of Corporate Governance is becoming more and more pronounced. An International

24 Parmjit Kaur, Globalisation: Corporate Governance and its position in India; Corporate Governance, Deep and Deep publications Pvt. Ltd, New Delhi 2003, P-102
conference was held in Kuala Lumpur in the year 1996. The basic objective was to comprehend the concept of Corporate Governance and start preparation for implementing all steps which will strengthen the foundations of Corporate Governance. The subject is now being talked about and taught in various educational institutions of higher learning. Several seminars and national conferences are being held on this topic. Indeed a high sense of enthusiasm has been witnessed in respect of Corporate Governance.

“Tangible steps have also been taken to strengthen logistics to Corporate Governance. These include release of “Code of Ethics relating to Directors of Companies and Secretaries of Companies”. Board aspects covering contents include the following:

**CODE OF ETHICS FOR DIRECTORS**

This code consists of five parts, namely, introduction, principles, Objectives, Definitions and code of Conduct. Code of Conduct has further been sub-divided into three parts, employees, creditors and customers (three points) and social responsibilities and the environment (five points).

**CODE OF ETHICS FOR COMPANY SECRETARIES**

This code consists of four parts, namely, Introduction, Principles, Objection and Code of Conduct. Five points govern the code of conduct.
The above two publications were released by Registry of Companies, Ministry of Domestic, Trade and Consumer Affairs, Malaysia in 1996.”25

PAKISTAN

Companies Ordinance, 1984 provides the basis for formal structure of Corporate Governance in Pakistan. For Modarba Companies, Corporate Governance structure has been laid down in Modarba Companies Ordinance, 1980 together with Rules made there under.

Some of the important points in respect of Governance are tabulated below:

PAKISTAN : SOME POINTS REGARDING CORPORATE GOVERNANCE

“1. Accountability – Accountability of Management is expected to be enforced through annual general meeting by the shareholders. This requires excellent education of shareholders and management which, in most of the cases in Pakistan, appears to be an agenda of tomorrow. Corporate culture for efficient performance is the crying need and logistical steps need to be taken for ensuring healthy trends in accountability. Malpractices of some groups have marred the position and shareholders have remained deprived of their legitimate rights of receiving dividends.

2. Directors - Directors are to be elected by shareholders and after expiry of prescribed period, they will, subject to the Companies Ordinance, 1984 and the Articles of Association, seek fresh mandate. Their role requires delivery of genuine and true stewardship to shareholders.

3. External Auditor - External Auditors in Pakistan carry out audit. This is generally known as “Attest Function”. An improved outlook is needed to meet revising expectations of users.

4. Corporate Laws - Companies Ordinance, 1984 and several other Corporate laws govern corporate sector. Company Law Commission was set-up to review the corporate laws and focus attention on Corporate Governance. The Report was submitted in 1998.

   Efforts are going on for strengthening Corporate Governance foundations, improving corporate laws, developing an enlightened corporate culture and enforcing accountability in corporate laws.”

CORPORATE GOVERNANCE IN SOUTH AFRICA

“In South Africa which has some distinctive features in terms of the style of C.G. was produced in 1994 by the king committee, chaired by Mervyu King, a

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26 Parmjit Kaur, Globalisation: Corporate Governance and its position in India, Deep and Deep publications Pvt. Ltd, New Delhi 2003, P-103

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former advocate and judge of the Supreme Court of South Africa. Under South African company law, a company director is not a servant of the shareholders, but an autonomous organ of the company and acting on the company’s behalf. South African companies are expected to consider social, ethical and environmental issues. As a matter of fact the king committee covered worker’s participation, affirmative action programmes and code of ethics.”

FRANCE

“The French equivalent of the Cadbury Report, the Vienot Report was published in 1995 and its Dutch equivalent, the Peter’s Reports, was published in 1996. Belgium set-up its governance committee in 1997.”

CORPORATE GOVERNANCE IN BANGLADESH

“The practice of Corporate Governance in Bangladesh is of recent origin and is still in an evolutionary phase. The corporate sector country is governed by the Companies Act, 1994 and it does not have a long history, (Jamal Uddin Ahmed and M.A. Baree in corporate governance). For Transparency and Accountability observed that motivation instead of compulsion is what is required for the corporate sector in Bangladesh to accept and adopt a Corporate Governance Framework.”

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BRAZIL

A major concern for emerging economies like Brazil is the availability of long term finance, at competitive rates, for private sector development. The luck of such finance is widely considered an important handicap for the competitiveness of Brazilian industry especially in those sectors dominated by locally-owned enterprises that face greater difficulty accessing foreign capital markets. There is considerable scope for the exportation of minority shareholders in Brazil’s system of corporate governance. As a result investors may be less willing to provide finance to corporations. It is therefore hoped that the improvement of the legal and institutional framework that regulates the relationships of minority shareholders and lenders with controlling shareholders of corporations will foster the development of local capital markets. The approval in the lower chamber of the Brazilian congress of a new corporate law, granting greater protection to minority shareholders, has gained importance in the business and political communities.

“The privatization process initiated in the early 1990s, the growing role and activism of institutional investors and the influx of foreign capital in the stock exchange were expected to produce important effects in Brazilian corporate Governance. The new arrangements that emerged in this process continued to be characterised by a high degree of ownership concentration,
although control in some privatized firms is shared among a small group of shareholders. In many cases where the privatized firm was acquired by a multinational company, a process of buying the remaining shares from minority shareholders followed, reducing the liquidity of the firm’s shares in the market. Foreign investors generally avoided adopting a more activist stance, probably afraid of the complicated and inefficient Brazilian legal system.

The long period of time and the concessions required for the approval of Brazil’s new corporate law is clearly a test to the importance of resistances to change in the structure of corporate governance in Brazil. Another important obstacle is the nature of Brazil’s legal system. All administrative processes, judged by the local securities exchange commission (CVM) may be brought to courts, where a final resolution is always long and frequently costly.”

CORPORATE GOVERNANCE IN INDIA

“In India, the question of corporate governance has come up mainly in the wake of economic liberalization and deregulation of Industry and business as well as the demand for a new corporate ethos, and sticker compliance with the law of the land. In the context of the unique situation in India where the financial institutions hold substantial stakes in companies, the accountability of the directors including non-executives and nominees, has come into sharp focus.

30 www.yahoo.com
In recent years the debate on corporate governance has been stimulated by work in the area by the Governance of India, the SEBI and Confederation of Indian Industry (CII). The Kumar Mangalam Committee Report on corporate governance can justifiably be viewed as well thought out response to our need for better corporate governance. In May 1999 it set-up the Kumar Mangalam Committee.”31

A few years back, the Confederation of India Industries (CII) had issued a corporate governance code. The CII Charter on Corporate Governance includes the following points:

- A single board which should meet at least six times a year, preferably at an interval of two months.
- A listed company with a turnover of Rs.100 crore and above should have professionally competent, independent, non-executive directors who should constitute atleast 30 per cent of the board if the chairman of the company is a non-executive director and at least 50 per cent of the board if the chairman and managing director is the same person.
- No single person should hold directorship in more than 10 listed companies.
- The non-executive directors should actively participate in the board with clearly defined responsibilities. They should know how to read the balance sheet, profit and loss account, cash flow statements, etc. They should have some knowledge of the company law.

• The company should pay a commission over and above the sitting fees to the non-executive directors.

• Attendance record should be considered while reappointing directors.

• The Board should be provided with following key informations:
  ➢ Annual operating plans and budgets along with long-term plans.
  ➢ Capital, manpower and overhead budgets.
  ➢ Quarterly results of the company as a whole and its operating divisions.
  ➢ Internal audit reports.
  ➢ Various notices from revenue authorities.
  ➢ Accidents, pollution problems, etc.
  ➢ Default in payment of interest or non-payment of principal on any public deposit or secured creditors.
  ➢ Defaults in payment of inter-corporate
  ➢ Any issue which involves possible public or product liability claims.
  ➢ Details of any joint venture or collaboration agreements.
  ➢ Transactions to involve substantial payment towards goodwill, brand equity, etc.
  ➢ Recruitment or remuneration of senior officers below the board level.
  ➢ Labour problems and solutions and
  ➢ Quarterly details of foreign exchange exposure.

• Listed companies with either a turnover of over Rs.100 crore or paid up capital of Rs.20 crore should set-up audit committees within two years. The
Audit Committee should assist the board in accounting and reporting functions, should periodically interact with the statutory auditors and internal auditors and discharge their fiduciary responsibilities with due diligence.

- The listed companies should give data on:
  - high and low monthly average of share prices in a major stock exchange and
  - greater details on business segments, up to 10 per cent of turnover, sales revenue, etc.

- Major stock exchange should insist on a compliance certificate signed by the CEO and CFO stating that the management is responsible for the preparation and impeccability of the financial statements and other information on the annual reports, that its accounting policies confirm to standard practice and that the board has overseen the company’s system of international accounting and administrative controls either directly or through the audit committee.

- If any company goes to more than one credit rating agency it must divulge all the previous ratings.

- Companies that default on fixed deposits should not be permitted to accept further deposits and make inter-corporate loans or investments or declare dividends until the default is made goods.
TABLE 2.1

STATUS OF CORPORATE GOVERNANCE IN THE UNITED STATES OF AMERICA

<table>
<thead>
<tr>
<th>DEVELOPED WORLD</th>
<th>UNITED STATES</th>
</tr>
</thead>
</table>
| I. Legal Framework | • Based largely on incorporation laws in different states with commonality achieved through the Model Business Corporation Act (MBCA) published by American Bar Association (ABA).  
• Public Accounting Reform and Investor protection Act, 2002 (Sabanes-Oxley Act). |
| II. Regulatory Bodies | • Securities and Exchange Commission (SEC)  
• Stock Exchanges (Amex, NASDAQ and NYSE). |
| III. Institutional Bodies | • National Association of corporate Directors (NACD)  
• American Bar Association (ABA)  
• Association of Corporate Council  
• The Business Roundtable (BRT) |
The legal framework of the United States is based on the Model of Business Corporation Act (MBCA). Sarbanes-Oxley Act provides a mechanism for rebalancing the power between the board of directors, and top management. The certification of the financials by the CEO as required by the Act can be delegated to other officials, notably the CFO and the controller, who are more knowledgeable concerning the accuracy of the financial reports. The one major area where a lot of grounds is covered is director development activity. While making it mandatory may not be in the best interest of the process, the companies and institutions shall form a body to impart periodical training and development programmes to improve the quality of directors and the board process.
and practices. The National Association of Corporate Directors (NACD) in the United States assumes this responsibility.

The United States has chosen to enact a law in the form of Sarbanes-Oxley Act, mainly because that was required to create confidence in the minds of the investors and public in view of the major failures like Enron and WorldCom, which resulted in wholesale erosion of confidence in the whole governance process that prevailed till then. The board structure is unitary and it has independent audit, compensation and nomination committees on board. All the codes of corporate governance are envolved by institutional bodies such as National Association of corporate Directors (NACD), American Bar Association (ABA), Association of Corporate Council, The Business Roundtable (BRT), Council of Institutional Investors (CII), Institutional Shareholder Service (ISS). All the laws relating to corporate governance centre around disclosure and it is the major means of achieving transparency. NYSE, NASD, NACD, and ISS take active role in the development of directors development activity. The three corporate governance rating institutions play a major role in the rating process.

**Table 2.2**

**STATUS OF CORPORATE GOVERNANCE IN THE UNITED KINGDOM**

<table>
<thead>
<tr>
<th>UNITED KINGDOM</th>
<th>Common to England, Wales, Scotland and Northern Ireland</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Legal Framework</td>
<td>• Essentially a common law system</td>
</tr>
<tr>
<td></td>
<td>• European Union laws also followed.</td>
</tr>
<tr>
<td></td>
<td>• Listing Rules</td>
</tr>
</tbody>
</table>
| II. Regulatory Bodies | • Financial Services Authority (FSA)  
• the UK Listing Authority (UKLA)  
• Financial Reporting Council (FRC)  
• and its subsidiary Financial Reporting Review Panel (FRRP)  
• London Stock Exchange (LSE). |
| --- | --- |
| III. Institutional Bodies | • National Association of pension Funds (NAPF)  
• Confederation of the British Industry (CBI)  
• Institute of Chartered Secretaries and Administration (ICSA)  
• Institute of Directors (IOD). |
| IV. Board Structure | • Unitary  
• Separation of Roles of Chairman and CEO  
• Compensation, Audit and Nomination Committees with majority independent directors. |
| V. Codes | • Cadbury Report (1992)  
• Hampel Report and Combined code (1998)  
• Turnbull Report (1999)  
• Higgs Report and Revised Combined code (2003) |
| VI. Disclosure and Transparency | Centre around remuneration, reporting and audit. |
| VII. Director Development Activity | • IOD  
• 3i  
• ICSA |
| VIII. Corporate Governance Rating | Not available |

Source: [www.yahoo.com](http://www.yahoo.com)

It is understood from the above table that the UK corporate governance emphasizes board engagement with shareholders and compliance with a voluntary code of best practice. This promotes high standards of corporate governance behavior without stifling wealth creation. However there are no grounds for complacency. The regulatory burden imposed on boards should be carefully monitored. An excessive focus on
compliance – rather than issues of strategy and value-creation-undermines the viability of the UK’s unitary board concept.

The UK approach to “best practice” in corporate governance reflects the belief that the governance should promote both accountability to shareholders and the board’s ability to manage the company effectively.

A unitary board with members is collectively responsible for leading the company and division of powers at the top of the company. Running the board and running the company are two distinct roles. The chairman is responsible for running the board. The CEO is responsible for running the company. There are formal and transparent procedures for appointing directors, with all the appointments ratified by shareholders with regular evaluation of the effectiveness of the board and its committees. A close relationship between the board and shareholders exists so that the former understands the latter’s opinions and concerns. Separate resolutions on all substantial issues at general meetings are allowed to shareholders to express their opinions on individual items.

It also acknowledges that there is a strong commonality of interest between companies and shareholders that should be encouraged by giving shareholders a central role in the enforcement of corporate governance standards whereas regulators find it difficult to allow exceptions – as they must be seen to be applying rules consistently.
### Table 2.3
**STATUS OF CORPORATE GOVERNANCE IN GERMANY**

<table>
<thead>
<tr>
<th>GERMANY</th>
<th></th>
</tr>
</thead>
</table>
| **I. Legal Framework**                                                  | - The introductory Act to Civil code  
- The Civil code  
- The Commercial code  
- The Insolvency Act  
- The law on Limited Liability Companies.  
- The Stock Exchange Corporation Act.  
- The Law on the Registered Shares and the Relief of the Exercise of voting Rights (2001)  
- Law concerning supervisory board Access to information and independence of the company’s auditors  
- The Capital Raising Promotion Act.  
- The Law of Limited Liability Partnership. |
| **II. Regulatory Bodies**                                               | Sole entity responsible is The District Court- Commercial Register                                                                                                                                   |
| **III. Institutional Bodies**                                           | Not Present                                                                                                                                                                                    |
| **IV. Board Structure**                                                 | Two-Tier-supervisory Board with employee representation – Management Board (the executive).                                                                                                      |
| **V. Codes**                                                            | - The Berlin Initiative code (2000)  
| **VI. Disclosure and Transparency**                                     | Accounting principle based on Commercial prudence                                                                                                                                                |
| **VII. Director Development Activity**                                  | Very few organized ones.                                                                                                                                                                          |
The above table clearly reveals that the aim of the German Corporate Governance Code is to make Germany’s corporate governance rules transparent for both national and international investors and to strengthen confidence in the management of German corporations. The code addresses all major criticisms – especially from the international community namely inadequate focus on shareholder interests; the two-tier system of executive board and supervisory board; inadequate transparency of German corporate governance; inadequate independence of German supervisory boards and Limited independence of financial statement auditors.

The Government Commission on the German Corporate Governance Code remains in existence after the Code has been handed over. It will observe the development of corporate governance in legislation and practice and reviews the Code at least once a year for possible adaptation. Stock corporations or public companies limited by shares are regulated under the Stock Corporation act. This act contains binding rules concerning the foundation and constitution of such corporations, the organs and their duties, the rights of shareholder, rules concerning the (fixed) capital of the corporation, the issuance of shares and the dissolution of the company.
## TABLE 2.4

### STATUS OF CORPORATE GOVERNANCE IN BRAZIL

<table>
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<th>B . DEVELOPING NATIONS</th>
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</thead>
<tbody>
<tr>
<td><strong>BRAZIL</strong></td>
</tr>
</tbody>
</table>

| I. Legal Framework     | Brazilian Corporations Law (Law 6404 of 1976, and amendments Law 9457 of 1997 and Law 10303 of 2001); Directors not personally liable; Fiscal Council is necessitated by law which monitors the acts of the board members and the officers and reviews the management accounts and reports. |
| II. Regulatory Bodies  | The Brazilian Securities and Exchange Commission (BSEC). |
| III. Institutional Bodies | • Sao Paulo Stock Exchange (BOVESPA)  
• The Brazilian National Economic and Social Development Bank (BNDS)  
• The Instituto Brasileriro de Governance Corporation (IBGC) |
| IV. Board Structure    | • Unitary  
• Committees are rare. |
| V. Codes               | • Code of Best Practices (evolved by IBGC)  
• Recommendation on Corporate Governance (CVM) |
| VI. Disclosure and Transparency | Audited financial statements to be published. |
VII. Director Development Activity

Mostly under IBGC’s initiative and large numbers of directors trained since 1998.

VIII. Corporate Governance Rating

Not available.

Source: www.yahoo.com

It is quite clear that there is considerable scope for the expropriation of minority shareholders in Brazil’s system of corporate governance. The Sao Paulo Stock Exchange (BOVESPA) has also recently introduced a structure very similar to that of the German Neue Markt in the hope of stimulating Brazilian firms to adopt better government practices. All administrative processes judged by the local securities exchanges commission (VCVM) may be brought to courts, where a final resolution is always long, and frequently costly. Recommendations on Corporate Governance (CVM) are given to stock exchange, government, shareholders and other stakeholders as part of protecting investors rights. Audited financial statements are not disclosed, and is still to be brought to light. Though the board is unitary it has no committees on corporate governance. Hence the need to strengthen corporate governance is considered important.

**TABLE 2.5**

**STATUS OF CORPORATE GOVERNANCE IN MALAYSIA**

| MALAYSIA | Based on the UK Common Law Principles  
|----------|---------------------------------|
| I. Legal Framework | - The Companies Act, 1965  
| | - The Security Industry Act (SIA), 1983  
| | - The Securities Commission Act (SCA) 1993  
| | - Kuala Lampur Stock Exchange (KLSE) listing requirements.  |

| II. Regulatory Bodies | - The Securities Commission (SC)  
| | - Kuala Lumpur Stock Exchange (KLSE) and  
| | - The Companies Commission of Malaysia (CCM).  |

| III. Institutional Bodies | - Malaysian Institute of Corporate Governance (MICG) 1998 and  |
| IV. Board Structure | Unitary  
Audit, Nomination and Remuneration Committees. |
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<td>V. Codes</td>
<td>The Malaysian code on Corporate Governance (2002.)</td>
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</table>
| VI. Disclosure and Transparency | Annual reports and quarterly financial statements  
Statements of Internal Controls and Conformation to International Accounting Standards. |
| VII. Director Development Activity | Mandatory Accreditation Program (MAP) for directors of listed Companies. All directors of listed companies must have undergone MAP training.  
Corporate Directors Training Programme (CDTP) launched in 2001 and those who attend CDTP are exempted from MAP.  
Continuing Professional Education (CPE) offers regular training for directors. |
| VIII. Corporate Governance Rating | Not available. |

Source: [www.yahoo.com](http://www.yahoo.com)

Malaysia is seen as a worthy example of a ‘tiger economy’, experiencing continuous economic growth and social development. The Malaysian government itself is advocating improved corporate governance practices as a vital reform and a way of making the country resilient to any future financial crises. In assessing corporate governance issues it is found that legal protection for shareholders in these countries is
inadequate. It is noted that, although laws concerning shareholder rights and the regulatory framework in Malaysia appeared comprehensive and are relatively adequate compared to other countries, shareholder rights are often neglected in practice because of the excessive power enjoyed by controlling shareholders. Increased transparency in the form of disclosure with more extensive corporate requirements is unnecessary as markets provide optimal incentives for disclosure.

Enhanced standards of corporate governance and transparency will increase the attractiveness of the public listed companies thus making it easier to raise capital --- (and) more attractive as investment options --- (also) the revamped listing requirements are on a par with the rules of other exchanges in developed markets and this should serve to attract more international investors --- (and) afford greater protection to shareholders

**TABLE 2.6**

**STATUS OF CORPORATE GOVERNANCE IN INDONESIA**

|--------------------|--------------------------------------------------------------|
| II. Regulatory Bodies | • Bank of Indonesia (BOI) (for banks)  
                      • Jakarta Stock Exchange (JSE)  
                      • Surabaya Stock Exchange (SSE) and  
                      • Capital Market Supervisory Agency (CMSA) |
| III. Institutional Bodies | • National Committee for Corporate Governance Policies. |
### IV. Board Structure
- Dual Board Structure – The Board of Commissioners (Supervisory Board) the Board of Directors (executive Board) and
- Audit Committee mandatory; remuneration and nomination committees desirable.

### V. Codes
Guidelines by National Committee for Corporate Governance policies.

### VI. Disclosure and Transparency
- Audited annual reports mandatory and
- No disclosure on internal controls.

### VII. Director Development Activity
Half –a- dozen institutions offer training programmes but no mandatory requirements.

### VIII. Corporate Governance Rating
Not available.

**Source:** [www.yahoo.com](http://www.yahoo.com)

The Indonesian company law of 1995 is the most important framework for current legislation on Corporate Governance. In Indonesian company law the directors and commissioner represent the company. It has legal regulating frame work for disclosing misleading financial statement. The second major regulatory frame work, that
is Indonesian capital market law, applies to all Indonesian limited liability companies
capital market rules and regulations applicable to public companies as defined in the
company law. Indonesian Transparency Society discloses all material information both
mandatory and non mandatory. This Indonesian corporate Governance does not disclose
on internal controls. Director Development Activity offers training programmes to many
institutions for the benefit of the company.

TABLE 2.7
STATUS OF CORPORATE GOVERNANCE IN INDIA

| I. Legal Framework               | • Companies Act, 1956, and the amendments therein over the years, administered by DCA
|                                | • Securities Contract (Regulation) Act, 1956 (SCRA)
|                                | • Sick Industrial Companies (Special Provisions) Act, 1985 (SICA) and
|                                | • Securities and Exchange Board of India (SEBI) Act 1992
| II. Regulatory Bodies           | • Department of Company Affairs (DCA)
|                                | • Securities and Exchange Board of India (SEBI)
|                                | • Reserve Bank of India (RBI) for banks and
|                                | • Stock Exchange (Bombay Stock Exchange (BSE), National Stock Exchange (NSE), and other
|                                | Regional Stock Exchange which have become more or less defunct.)
| III. Institutional Bodies       | • Confederation of Indian Industry (CII)
|                                | • Institute of Directors (IOD)
| IV. Board Structure             | • Unitary
|                                | • Audit Committee with majority independent directors mandatory. Remuneration and nomination
The above table reveals the governance practices in India. We can observe that our governance practices are very much similar to most of the developed nations like the US and the UK. It has corporate governance codes as part of the listing agreement with the stock exchange and/or under the general commercial laws. Most countries have evolved
codes out of necessity to improve governance in a changing global economic scenario and they have usually come from industry rather than from regulator or government. In India too, the first initiative was from an industrial body, confederation of Indian Industry (CII).

Three of the rating agencies in India have evolved corporate governance rating methods. While our disclosure and transparency practices have considerably improved, there are still grey areas like ownership details. Reports while showing ownership details continue to mention persons acting in concert with the promoter holding. The regulatory agencies which protect the investor are investors’ Grievances and Guidance Division of SEBI, Department of Company affairs, Department of Economic affairs, Reserve Bank of India, Consumer courts and courts of law. Every stock exchange has to have a grievance redressal mechanism in place and an investor protection fund. The CII Desirable Code (1998), K.M.Birla Committee Report (2000), Naresh Chandra Committee Report (2002) and Narayana Murthy Committee Report (2003), also play an important role in corporate governance as retail investors look upon them for positive use of investors voting rights.

While SEBI has a bigger role to play in the practices and processes of governance, the structure for governance shall be vested with DCA. SEBI has actually nothing to do with the structure formation or composition of the board. SEBI has actually nothing to do with the structure formation or composition of the board. Such aspect shall be vested with DCA since all incorporation regulations are monitored and controlled by DCA. Hence any recommendation or guideline regarding the structure
such as formation of board, independent component, committees etc. shall come under the purview of DCA and not SEBI.

THE ANGLO – AMERICAN MODEL

This is also known as unitary board model, in which all directors participate in a single board comprising both executive and non-executive directors in varying proportions. This approach to governance tends to be shareholder-oriented. It is also corporate the ‘Anglo –Saxon’ approach to Corporate governance, being the basis of corporate governance in America, Britain, Canada, Australia and other Commonwealth law countries including India.

The major features of the Anglo –Saxon or Anglo –American model of corporate governance are as follows:

i) The ownership of companies is more or less equally divided between individual shareholders and institutional shareholders.

ii) Directors are rarely independent of management.

iii) Companies are typically run by professional managers who have negligible ownership stakes. There is a fairly clear separation of ownership and management.

iv) Most institutional investors are reluctant activists. They view themselves as portfolio investors interested in investing in a broadly diversified portfolio of liquid securities and

v) The disclosure norms are comprehensive, the rules against insider trading tight, and the penalties stiff, all of which provide adequate protection to the
small investor and promote general market and liquidity. Incidentally they also discourage large investors from taking an active role in corporate governance.

GERMAN MODEL

This model also known as the two –tier model, Corporate governance is exercised through two boards, in which the upper board supervises the executive board on behalf of stakeholders. This approach to governance is typically more societal – oriented and is sometimes called the continental European approach, being the basis of corporate governance adopted in Germany, Holland, and to an extent, France.

In this model although the shareholders own the company, they do not entirely dictate the governance mechanism. Shareholders elect 50 per cent of members of supervisory board and the other half is appointed by labour unions. This ensures that employees and labourers also enjoy a share in the governance. The supervisory board appoints and monitors the management board. There is a reporting relationship between them, although the management board independently conducts the day-to-day operations of the company.

THE JAPANESE MODEL

This is business network model, which reflects the cultural relationships seen in the Japanese keiretsu network, in which boards tend to be large, predominantly executive and often ritualistic. The actual power in the enterprise lies in the
relationship between top management in the companies in the Keiretsu network. The approach bears some comparison with Korean chaebol.

In the Japanese model the financial institution has an accrual role in governance. The shareholders appoint the board of directors and the president. The distinctive features of the Japanese corporate governance mechanism are as follows:

- The President who consults both the supervisory board and the executive management is included.
- Importance of the lending bank is highlighted.

CONCLUSION

We can conclude that measures taken to restore trust in some instances over reacted in order to satisfy social demands, burdening business with greater reporting requirements for no discernible benefit for stakeholders. However much of the changes have been positive and helped to make firm operations much more transparent particularly in developing nations, although it is difficult to measure the impact this has on investment decisions by investors. There remain considerable contextual distinctions across nations, making a universal expression of corporate governance rules unlikely in the current circumstances. These rules will, no doubt, have to be reconciled or aligned in some respect in due course, as globalization and international business activities grow.