CHAPTER 2
PRINCIPLES AND PRACTICES OF CORPORATE GOVERNANCE

In this chapter the Principles and Practices of Corporate Governance is discussed and defined to have a clear understanding of the terms, concepts, ideas, rules and regulations, enforcement agencies, and the expected practice by the corporate sector in India.

Organization for Economic Cooperation and Development (OECD) along with the World Bank and the International Finance Corporation brought out the following six principles of Corporate Governance to be implemented by the member countries and the other countries that have global access.

Ensuring the Basis for an Effective Corporate Governance Framework: The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities.

The Rights of Shareholders and Key Ownership Functions: The corporate governance framework should protect and facilitate the exercise of shareholders' rights.

The Equitable Treatment of Shareholders: The corporate governance framework should ensure the equitable treatment of all shareholders including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights.

The Role of Stakeholders in Corporate Governance: The corporate governance framework should recognize the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs and the sustainability of financially sound enterprises.

5. Disclosure and Transparency: The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and governance of the company.

6. The Responsibilities of the Board: The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board’s accountability to the company and the shareholders.

The Principles and Practices vary on the basis of Politics, Economics, Culture, and Ethics of the people in a country. The OECD principles provide a basic structure for implementation of Corporate Governance Practices. Corporate Governance norms in India also include the essence of above principles. The main aspects or attributes have been identified which are common and very essential for the success of Corporate Governance in India and elsewhere in the world.

7. Investor Relations: The Company has to maintain good relationship with investors by active cooperation with shareholders by attending to their grievances and informing them in time about the meetings and important decisions to be made.

8. Board Structure and System: The Board has a great role in the implementation of corporate governance by securing good performance from top management and protecting the interest of the shareholders. Composition of Board with a portion of Non-Executive Independent Directors with adequate knowledge, experience and integrity is required for achieving good investor relations and enhancement of stakeholders’ value.

9. Stakeholders’ Value: Stakeholders are those who are interested in the success and development of the company. They are: Employees, Creditors, Suppliers, Customers, Society and the Government. The successful implementation of Corporate Governance practice enhances their value.

10. Transparency and Disclosure: True, correct, complete and timely information is required for right decisions. Corporate Governance practice ensures the provision of complete and timely information through Annual Reports, News release, Newspapers and company website for the purpose of making good decisions.
1. Performance of the Company in terms of compliance and financial results: The main aspect of corporate governance is complying with all the rules and regulations of the Government and the Government Agencies. This ensures the successful overall performance of the company and good financial results.

1.1 Investor Relations

Corporate governance is basically a system of relationships among participants in the corporate system. The shareholders being the providers of risk bearing capital deserve special attention to their interests. An investor is one who invests hard earned money in shares and securities with the expectation of financial return. The investors want to know about the company and the Board is expected to know how the investors perceive about their companies. The shareholders are the owners of the company but they are separate from the company. The board of directors is elected by the shareholders to oversee, govern management and to make corporate decisions on their behalf. As a result, the board is directly responsible for protecting and managing shareholders' interests in the company. The ultimate responsibility for the protection of shareholder value lies with each individual investor. The investor is responsible for reviewing corporate policy and governance as well as the compensation of managers. The market or the securities of a company depends upon the confidence of the investors.

It needs to be noted that the boards that strive for active co-operation between corporations and shareholders are most likely to create wealth, employment and sustainable economies.82

2.1.1. Types of investors:

1. Controlling shareholders: Individuals, a family or a holding company may hold a large bulk of shares. By virtue of their substantial shareholding, they may influence the company and get representation on the Board.

2. Individual shareholders: It represents a widely scattered group of individuals holding small number of shares. They are known as minority shareholders. They do not have any significant voice in the corporation except at the general meetings. The development of a

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sound corporate governance system provides for the effective participation by minority shareholders. The recently introduced postal ballot in India has given the non-controlling shareholders an increased opportunity to participate in corporate decision making.

Institutional shareholders: They represent an organized and motivated group. They contribute to improve the quality of corporate governance as they are concerned about obtaining fair treatment form management and majority shareholders.

2. Protection of the Rights of Shareholders and Key Ownership Functions:

Corporate Governance practices ensure that the Shareholders rights are protected and her facilitate the exercise of shareholders’ rights.

Basic shareholder rights include;
secure methods of ownership registration,
transfer and transmission of shares,
obtain relevant and material information about the companies on a timely and regular basis,
participate and vote in general shareholder meetings,
elect and remove members of the board and share in the profits of the companies.

Shareholders should have the right to participate in, and to be sufficiently informed on decisions concerning fundamental corporate changes such as:

1) amendments to the statutes, or articles of incorporation or similar governing documents of the company,

2) the authorization of additional shares and

3) extraordinary transactions, including the transfer of all or substantially all assets that in effect result in the sale of the company.
Shareholders should have the opportunity to participate effectively and vote in general shareholder meetings and should be informed of the rules, including voting procedures that govern general shareholder meetings:

Shareholders should be furnished with sufficient and timely information concerning the date, location and agenda of general meetings, as well as full and timely information regarding the issues to be decided at the meeting.

Shareholders should have the opportunity to ask questions to the board, including questions relating to the annual external audit, to place items on the agenda of general meetings, and to propose resolutions, subject to reasonable limitations.

Effective shareholder participation in key corporate governance decisions, such as the nomination and election of board members, should be facilitated. Shareholders should be able to make their views known on the remuneration policy for board members and key executives. The equity component of compensation schemes for board members and employees should be subject to shareholder approval.

Shareholders should be able to vote in person or in absentia, and equal effect should be given to votes whether cast in person or in absentia.

Capital structures and arrangements that enable certain shareholders to obtain a degree of control disproportionate to their equity ownership should be disclosed.

Markets for corporate control should be allowed to function in an efficient and transparent manner.

The rules and procedures governing the acquisition of corporate control in the capital markets, and extraordinary transactions such as mergers, and sales of substantial portions of corporate assets, should be clearly articulated and disclosed so that investors understand their rights and recourse. Transactions should occur at transparent prices and under fair conditions that protect the rights of all shareholders according to their class.
Anti-take-over devices should not be used to shield the management and the board from accountability.

The exercise of ownership rights by all shareholders, including institutional investors, should facilitated.

Institutional investors acting in a fiduciary capacity should disclose their overall corporate governance and voting policies with respect to their investments, including the procedures that they have in place for deciding on the use of their voting rights.

Institutional investors acting in a fiduciary capacity should disclose how they manage material conflicts of interest that may affect the exercise of key ownership rights regarding their investments.

Shareholders, including institutional shareholders, should be allowed to consult with each other on issues concerning their basic shareholder rights as defined in the Principles, subject to exceptions to prevent abuse.

1.3. Equitable Treatment of Shareholders:

The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the portunity to obtain effective redress for violation of their rights.

All shareholders of the same series of a class should be treated equally.

1. Within any series of a class, all shares should carry the same rights. All investors should be able to obtain information about the rights attached to all series and classes of shares before they purchase. Any changes in voting rights should be subject to approval by those classes of shares which are negatively affected.

2. Minority shareholders should be protected from abusive actions by, or in the interest of, controlling shareholders acting either directly or indirectly, and should have effective means of redress.
3. Votes should be cast by custodians or nominees in a manner agreed upon with the beneficial owner of the shares.

4. Impediments to cross border voting should be eliminated.

5. Processes and procedures for general shareholder meetings should allow for equitable treatment of all shareholders. Company procedures should not make it unduly difficult or expensive to cast votes.

6. Insider trading and abusive self-dealing should be prohibited.

7. Members of the board and the key executives should be required to disclose to the board whether they, directly, indirectly or on behalf of third parties, have a material interest in any transaction or matter directly affecting the corporation.83

1.4. Requisites for Good investor relations84

1. Registration of transfer and transmission within a short period of time from the date of lodgment of valid transfer documents.

2. Quick response to investor’s queries.

3. Prompt remittance of dividend to the investors.

4. Dematerialization facility.

5. Extending courteous and hospitable reception to investors visiting the Investor Service Centre of the Company.

6. Equipping Investor Service Centre with best of communication and information technology facilities and manning these with personnel proficient in public relations.

7. Ensuring that investors receive the necessary information through e-mail, fax, telephone or mail and avoid their having to visit the Investor Service Centre of the company.

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8. Ensuring transparency in disclosure of all material information through Annual Reports and other means of communication.

9. Being innovative and proactive in providing service so as to achieve the maximum investor satisfaction.

10. Effective procedures and policies with regard to the following:
    a. Stock Exchange listings
    b. Transfer and transmission of shares
    c. Simultaneous transfer and dematerialization
    d. Implementation of bank mandate for remittance of dividend to shareholders in a safe manner
    e. Providing bank details on dividend warrants
    f. Policy with regard to unclaimed dividends
    g. Splitting of share certificates
    h. Consideration of shareholdings
    i. Loss of share certificates
    j. Renewal of torn or mutilated certificates
    k. Information about financial results on website
    l. Communication of name and address of persons handling investor’s problems.

2.1.5. Investor Protection Measures:

SEBI was established with the primary objective of protecting the interest of the investors in the securities market.

1. SEBI can issue directions to all intermediaries and other persons associated with the securities market in the interest of the investors or for orderly development of the securities market.

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2. SEBI has notified the SEBI (Investor Protection and Education Fund) Regulations, 2009 with a view to strengthening its activities for investor protection. The fund shall be used for the following purposes:
   a. Educational activities including seminars, training, research and publications, aimed at investors.
   b. Awareness programmes through media - print, electronic, aimed at investors.
   c. Funding investor education and awareness activities of investor associations recognized by the Board.
   d. Aiding investor associations recognized by the Board to undertake legal proceedings in the interest of investors in securities that are listed or proposed to be listed.
   e. Exchanges have set up an Investor Protection Fund (IPF) to meet the claims of investors against defaulter members.
   f. SEBI (Disclosure and Investor Protection) Guidelines, 2000: The primary objective of Securities and Exchange Board of India (SEBI) has been investor protection. The Disclosure and Investor Protection guidelines apply to the primary market, i.e., public issues made by listed and unlisted companies, rights issues, and offers for sale by listed companies in certain cases.

2.1.6. **Investor Grievance Redressal Mechanism:**

1. SEBI and Stock Exchanges have set up investor grievance redressal cells for fast Redressal of investor complaints relating to securities markets.

2. SEBI has directed all the stock exchanges, registered brokers, sub-brokers, depositories and listed companies to make a provision for a special email ID of the grievance Redressal division/compliance officer for the purpose of registering complaints by the investors.
3. SEBI has set up a mechanism for redressal of investor grievances arising from the securities market.

4. SEBI provides "walk-in" service at its head office in Mumbai and its regional offices in New Delhi, Chennai, Kolkata and Ahmadabad on all working days. Investors can meet the officials and get guidance relating to the grievances that they may have against issuers. Investors can also meet the higher officials of SEBI on specified working days.

1.7 Investor Relations under clause 49 of Listing Agreement as per the SEBI Guidelines:

Clause 49 of the Listing Agreement has incorporated many provisions designed to promote better investor’s relations. The relevant provisions have been enumerated below:

a. Shareholders Grievance Committee: The Board has to constitute a committee under the Chairmanship of a Non-executive director to specifically look into shareholders’ and investors’ complaints relating to share transfers, non-receipt of copy of Annual Reports, non-receipt of declared dividend, etc., and to monitor investor grievances. The monitoring of share transfer process is to be done by an officer of committee or Recognized Transfer Agency.

b. Information of General Body meetings:
   1. Location and time and date where the last three AGMs were held
   2. Special resolution put to vote through postal ballot
   3. Details of voting pattern
   4. Persons who conducted the postal ballot
   5. Resolution proposed to be conducted through postal ballot
   6. Procedure for postal ballot

c. Means OF communication: Quarterly results and presentations made to analysts shall be posted on company’s website or shall be sent to stock exchange in a form that it may put the same on its website.
Information about Directors: In the event of appointment or reappointment of directors, the shareholders must be provided the following information:

i) A brief resume of the director.
ii) Nature of his expertise in specific functional areas.
iii) Names of the companies in which the person also holds directorships and the membership of the Committees of the Board.
iv) Shareholding of non-executive directors as stated in clause 49 (IV E) (v)

Clause 49 requires the provision of the following information to shareholders:
1. Particulars of AGM
2. Financial Calendar
3. Date of book closure
4. Dividend payment date
5. Name of stock exchanges where listed and stock code
6. Market price data and performance of company’s share in comparison to share price indices.

2 Board Structure and System

The Board has to monitor the company and its management on behalf of the shareholders. All corporate governance issues are implemented by the board. Without a good board, shareholders and other stakeholders may run undue risks along with the company. It is cause of its central role in the governance of the corporation that investors and the markets pay very close attention to the board structures and procedures that determine its operation.

2.1 Composition of Board86

1. The Board of directors of the company shall have an optimum combination of both Executive Directors and Non-executive Directors. Fifty percent of the board of directors shall be non-executive directors.

2. Where the Chairman of the Board is a non-executive director, at least one-third of the Board should comprise of independent directors and in case he is an executive director, at least half of the Board should comprise of independent directors.

3. For the purpose of the sub-clause (ii), the expression ‘independent director’ shall mean a non-executive director of the company who:

   a. apart from receiving director’s remuneration, does not have any material pecuniary relationships or transactions with the company, its promoters, its directors, its senior management or its holding company, its subsidiaries and associates which may affect independence of the director;
   b. is not related to promoters or persons occupying management positions at the board level or at one level below the board;
   c. has not been an executive of the company in the immediately preceding three financial years;
   d. is not a partner or an executive or was not partner or an executive during the preceding three years, of any of the following:
   e. the statutory audit firm or the internal audit firm that is associated with the company, and
   f. the legal firm(s) and consulting firm(s) that have a material association with the company.
   g. is not a material supplier, service provider or customer or a lessor or lessee of the company, which may affect independence of the director; and
   h. is not a substantial shareholder of the company i.e. owning two percent or more of the block of voting shares.

2.2 Board System:

Non executive directors’ compensation and disclosures:

All fees/compensation, if any paid to non-executive directors, including independent directors, shall be fixed by the Board of Directors and shall require previous approval of shareholders in general meeting. The shareholders’ resolution shall specify the limits for the maximum number of stock options that can be granted to non-executive directors, including dependent directors, in any financial year and in aggregate.
Other provisions as to Board and Committees:

The board shall meet at least four times a year, with a maximum time gap of three months between two meetings. The minimum information to be made available to the board is as given below: (Annexure – I A).

Annual operating plans and budgets and any updates.

Capital budgets and any updates.

Quarterly results for the company and its operating divisions or business segments.

Minutes of meetings of audit committee and other committees of the board.

The information on recruitment and remuneration of senior officers just below the board level, including appointment or removal of Chief Financial Officer and the Company Secretary.

Show cause, demand, prosecution notices and penalty notices which are materially important.

Fatal or serious accidents, dangerous occurrences, any material effluent or pollution problems.

Any material default in financial obligations to and by the company, or substantial nonpayment for goods sold by the company.

Any issue, which involves possible public or product liability claims of substantial nature, including any judgement or order which, may have passed strictures on the conduct of the company or taken an adverse view regarding another enterprise that can have negative implications on the company.

1. Details of any joint venture or collaboration agreement.

2. Transactions that involve substantial payment towards goodwill, brand equity, or intellectual property.
3. Significant labour problems and their proposed solutions. Any significant development in Human Resources and the Industrial Relations, such as signing of wage agreement, implementation of Voluntary Retirement Scheme etc.

4. Sale of material nature, of investments, subsidiaries, assets, which is not in normal course of business.

5. Quarterly details of foreign exchange exposures and the steps taken by management to limit the risks of adverse exchange rate movement.

6. Non-compliance of any regulatory, statutory or listing requirements and shareholders service such as non-payment of dividend, delay in share transfer etc.

b. of Directorship: A director shall not be a member in more than 10 committees or act as chairman of more than five committees across all companies in which he is a director. Furthermore it should be a mandatory annual requirement for every director to inform the company about the committee positions he occupies in other companies and notify changes as and when they take place.

Code of Conduct

The Board shall lay down a code of conduct for all Board members and senior management of the company. The code of conduct shall be posted on the website of the company.

All Board members and senior management personnel shall affirm compliance with the code on an annual basis. The Annual Report of the company shall contain a declaration to this effect signed by the CEO

2.3 CEO Duality and Corporate Governance

CEO duality refers to a situation where the CEO is also the chairperson of the board. The combination of these two positions has generated controversy. The board is responsible for hiring and firing CEOs and also for their performance appraisal. This particular aspect of relationship creates a problem.
It is likely that the firms with higher information asymmetry and those with higher agency costs may prefer split roles. Also, firms with higher debt or equity may opt for separate roles.

One view is that combined position deprives the board of its independence. It is also suggested that the CEO compensation increases as the board control decreases. It is necessary to determine the relative costs and benefits of CEO duality. It is assumed that each firm chooses an optimal mix of agency control mechanisms. For instance, if the existing monitoring mechanisms are effective, lower will be the benefit of splitting the positions. The relative costs and benefits of split decisions are affected by other factors such as; existing monitoring mechanisms, power of the CEO, degree of agency problem, and cost of information transfer, institutional ownership and block holders, and the boards dominated by outside directors.

2.4 Independent directors

“Independent directors are those who, apart from receiving director’s remuneration, do not have any material pecuniary relationship or transactions with the company, its promoters, its management or its subsidiaries, which in the judgment of the board may affect their dependence of judgment.”

Role of Independent Directors:

- To monitor and control the chairman/chief executive,
- To serve as a link with external environments,
- To provide an international perspective,
- To improve board processes,
- To bring in specialized knowledge,
- To provide continuity,
- To help identify alliances and acquisition, to help maintain an ethical climate, among others.
2.5 Director Training

The Indian Code passed the Companies Amendment Bill in 2003 which made director training mandatory. The training concept is evolved to non executive directors and the clause 49 talks about the training needs. One of the non mandatory requirements of clause 49 is in respect of training of board members which states as under:

“Company shall train its Board members in the business model of the company as well as the risk profile of the business parameters of the company, their responsibilities as directors, and the best ways to discharge them.”

Non Executive Directors (NED) could bring range of skills and experience to a company and can influence its decision making process. Some boards of directors are able to call upon independent external advisors (e.g. lawyers, accountants, etc.) to assist them in their work, in particular, in areas where there is potential for conflict of interest or where special technical skills are required (such as developing remuneration plans, or conducting board performance evaluations). The disclosure of the ability of the board to make use of such experts may indicate shareholders that the directors are informed and supported to the fullest extent possible.

2.6. Committees of the Board

The Board of the company places reliance on outside independent directors for monitoring the performance of the company and hence, the board sets up many committees, mainly consisting of independent directors such as:

Audit Committee
Compensation/Remuneration Committee
Nomination Committee
Shareholders & Investors Grievance Committee
Ethics and Compliance Committee
6.1 Audit Committee

Audit committee consisting of independent directors has to report to the board of directors. The committee works as a link between the external auditors and internal auditors. The main function of this committee is to review the audited and unaudited financial statements which are issued by the company. The committee shall discuss the financial aspects with the external auditors relating to any problems, qualifications if any, deviations in the accounting standards and other financial matters. They recommend the publication of results to the board for its approval.

Qualified and Independent Audit Committee

A qualified and independent audit committee shall be set up, giving the terms of reference subject to the following:

i. The audit committee shall have minimum three directors as members. Two-thirds of the members of audit committee shall be independent directors.

ii. All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise.

iii. The Chairman of the Audit Committee shall be an independent director;

iv. The Chairman of the Audit Committee shall be present at Annual General Meeting to answer shareholder queries;

v. The audit committee may invite such of the executives, as it considers appropriate (and particularly the head of the finance function) to be present at the meetings of the committee, but on occasions it may also meet without the presence of any executives of the company. The finance director, head of internal audit and a representative of the statutory auditor may be present as invitees for the meetings of the audit committee;
vi. The Company Secretary shall act as the secretary to the committee.

1. **Meeting of Audit Committee**

The audit committee should meet at least four times in a year and not more than four months shall elapse between two meetings. The quorum shall be either two members or one third of the members of the audit committee whichever is greater, but there should be a minimum of two independent members present.

2. **Powers of Audit Committee**

The audit committee shall have powers, which should include the following:

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

3. **Role of Audit Committee**

The role of the audit committee shall include the following:

1. Oversight of the company's financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct, sufficient and credible.

2. Recommending to the Board, the appointment, re-appointment and, if required, the replacement or removal of the statutory auditor and the fixation of audit fees.

3. Approval of payment to statutory auditors for any other services rendered by the statutory auditors.

4. Reviewing, with the management, the annual financial statements before submission to the board for approval, with particular reference to:
a. Matters required being included in the Director’s Responsibility Statement to be included in the Board’s report in terms of clause (2AA) of section 217 of the Companies Act, 1956

b. Changes, if any, in accounting policies and practices and reasons for the same

c. Major accounting entries involving estimates based on the exercise of judgment by management.

d. Significant adjustments made in the financial statements arising out of audit findings

e. Compliance with listing and other legal requirements relating to financial statements

f. Disclosure of any related party transactions

g. Qualifications in the draft audit report.

5. Reviewing, with the management, the quarterly financial statements before submission to the board for approval

6. Reviewing, with the management, performance of statutory and internal auditors, adequacy of the internal control systems.

7. Reviewing the adequacy of internal audit function, if any, including the structure of the internal audit department, staffing and seniority of the official, heading the department, reporting structure coverage and frequency of internal audit.

8. Discussion with internal auditors about any significant findings and follow up there on.

9. Reviewing the findings of any internal investigations by the internal auditors into matters where there is suspected fraud or irregularity or a failure of internal control systems of a material nature and reporting the matter to the board.

10. Discussion with statutory auditors before the audit commences, about the nature and scope of audit as well as post-audit discussion to ascertain any area of concern.
11. To look into the reasons for substantial defaults in the payment to the depositors, debenture holders, shareholders (in case of nonpayment of declared dividends) and creditors.

12. To review the functioning of the Whistle Blower mechanism, in case it is existing.

13. Carrying out any other function as is mentioned in the terms of reference of the Audit Committee.

**Review of information by Audit Committee**

The Audit Committee shall mandatorily review the following information:

1. Management discussion and analysis of financial condition and results of operations;

2. Statement of significant related party transactions (as defined by the audit committee), submitted by management;

3. Management letters / letters of internal control weaknesses issued by the statutory auditors;

4. Internal audit reports relating to internal control weaknesses; and

5. The appointment, removal and terms of remuneration of the Chief internal auditor shall be subject to review by the Audit Committee.

**6.2 Compensation / Remuneration Committee**

The shareholders are becoming more concerned about the disclosure and transparency of company in which they have invested their money and definitely would like to know the compensation / remuneration package of the directors and as well the senior management of the company. This committee, having regard to the long term goal of the company design a package for the directors and as well for the senior management which is a transparent policy and review remuneration/ compensation, approve wherever within its power, recommend for approval to board/shareholders and the disclosures are also made in the annual reports.
requirement of Clause 49 on Remuneration Committee:

1. 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.

2. To avoid conflicts of interest, the remuneration committee, which would determine the remuneration packages of the executive directors should comprise of at least three directors, all of whom should be non-executive directors, the chairman of committee being an independent director.

3. All the members of the remuneration committee should be present at the meeting.

4. The Chairman of the remuneration committee should be present at the Annual General Meeting, to answer the shareholder queries. However, it would be up to the Chairman to decide who should answer the queries.

1.6.3 Nomination Committee:

Nomination committee is normally set up to decide and select the new non executive director and it is headed by the Chairman along with other independent directors as members. The committee screens the prospective candidates for the position of non executive directors and makes its selection.

1.6.4 Shareholders & Investors Grievance Committee:

This committee is formed for overseeing the investor’s grievances and resolving the same. Clause 49 of the Listing Agreement prescribes the following in respect of this committee.

1. A board committee under the chairmanship of a non-executive director shall be formed to specifically look into the redressal of shareholder and investors complaints like transfer of shares, non-receipt of balance sheet, non-receipt of declared dividends etc. This Committee shall be designated as ‘Shareholders/Investors Grievance Committee’.
2. To expedite the process of share transfers the board of the company shall delegate the power of share transfer to an officer or a committee or to the registrar and share transfer agents. The delegated authority shall attend to share transfer formalities at least once in a fortnight.

3.6.5 Ethics and Compliance Committee

This committee reviews the ethical policy of the company and also keeps a close watch the code of conduct formulated by the board and its adherence by all the employees of the company. Further advises the board on ethics related matters, modifications of code of conduct.

3.7 The Responsibilities of the Board - OECD Principles

The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board’s accountability the company and the shareholders.

A. Board members should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the company and the shareholders.

B. Where board decisions may affect different shareholder groups differently, the board should treat all shareholders fairly.

C. The board should apply high ethical standards. It should take into account the interests of stakeholders.

D. The board should fulfill certain key functions, including:

1. Reviewing and guiding corporate strategy, major plans of action, risk policy, annual budgets and business plans; setting performance objectives; monitoring.

implementation and corporate performance; and overseeing major capital expenditures, acquisitions and disinvestments.

2. Monitoring the effectiveness of the company’s governance practices and making changes as needed.

3. Selecting, compensating, monitoring and, when necessary, replacing key executives and overseeing succession planning.

4. Aligning key executive and board remuneration with the longer term interests of the company and its shareholders.

5. Ensuring a formal and transparent board nomination and election process.

6. Monitoring and managing potential conflicts of interest of management, board members and shareholders, including misuse of corporate assets and abuse in related party transactions.

7. Ensuring the integrity of the corporation’s accounting and financial reporting systems, including the independent audit, and that appropriate systems of control are in place, in particular, systems for risk management, financial and operational control, and compliance with the law and relevant standards.

8. Overseeing the process of disclosure and communications.

E. The board should be able to exercise objective independent judgement on corporate affairs.

1. Boards should consider assigning a sufficient number of non-executive board members capable of exercising independent judgement to tasks where there is a potential for conflict of interest. Examples of such key responsibilities are ensuring the integrity of financial and non-financial reporting, the review of related party transactions, nomination of board members and key executives, and board remuneration.

2. When committees of the board are established, their mandate, composition and working procedures should be well defined and disclosed by the board.

3. Board members should be able to commit themselves effectively to their responsibilities.
F. In order to fulfill their responsibilities, board members should have access to accurate, relevant and timely information.

2.8. Measuring Board Performance:

"One of the prime responsibilities of any Chairman is to ensure that a company has a high-performing Board composed of high-performing directors. The Board Effectiveness Review and Charter of Expectations play a pivotal role in achieving this objective. Board evaluation has grown in prominence as a result of the revised Combined Code and many companies are facing this issue for the first time. Barclays has long recognized the importance of Board evaluation and as one of the first major UK companies to introduce a formal system of Board evaluation. It implemented a new, independently facilitated Board Effectiveness Review in 2004 and repeated the process, with minor modifications." Matthew W Barrett, Group Chairman, Barclays PLC Corporate Governance International Journal for enhancing board performance.

The Higgs suggestion for good practice, attached to the Combined Code in UK include some guidance on performance evaluation though the guidance does not go into detail about how the evaluation process should be conducted, nor what target measures of performance might be the evaluation. Only the following suggestions are made:

The board should state in the annual report how the evaluation had been conducted

Chairman is responsible for selecting an effective process of evaluation and action on its outcome.

Using third party for carrying out evaluation would bring objectivity to the process.

With the global best practice in mind, the clause 49 of Listing Agreement also talks as one of the non mandatory requirement on this subject while discussing the same under the head mechanism for evaluating non-executive board member. The extract from clause 49 states that:

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The performance evaluation of non-executive directors should be done by a peer group comprising the entire Board of Directors, excluding the director being evaluated and Peer Group evaluation should be the mechanism to determine whether to extend or continue the terms of appointment of non-executive directors.

1.9 Summary

The growth of any company would much depend upon the sense of direction and the pose of the board as a whole. The entire board and its constituents like CEO, Chairman, executive and non-executive directors shall discharge their main functions in the best interest of company. The roles and responsibilities with best global practices as members of the board members of Shareholders & Grievance Committee, Compensation/Remuneration committee, Audit Committee, nomination Committee and any other sub-committee of the board, will ensure statutory compliance in all matters.

Stakeholders’ Value

A corporate stakeholder is one who can affect or be affected by the actions of the business as a whole. The stakeholder concept was first used in a 1963 internal memorandum at Stanford Research Institute. It defined stakeholders as “those groups without whose support organization would cease to exist.” The theory was later developed and championed by R. Edward Freeman in the 1980s. The term has been broadened to include anyone who has an interest in a matter.

The main contender to value maximization as the corporate objective is called stakeholder theory”. Stakeholder theory says that managers should make decisions that take account of the interest of all the stakeholders in a firm. Stakeholders include all individuals or groups who can substantially affect, or be affected by the welfare of the firm-a category that includes not only the financial claimholders, but also employees, customers, communities, and government officials.

1.1 The Role of Stakeholders in Corporate Governance

The corporate governance framework should recognize the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders for the success of enterprises.

The rights of stakeholders that are established by law or through mutual agreements are to be protected.

Where stakeholder interests are protected by law, stakeholders should have the opportunity to gain effective redress for violation of their rights.

Performance-enhancing mechanisms for employee participation should be permitted to develop.

Where stakeholders participate in the corporate governance process, they should have access to relevant, sufficient and reliable information on a timely and regular basis.

Stakeholders, including individual employees and their representative bodies, should be able to freely communicate their concerns about illegal or unethical practices to the board and their views should not be compromised for doing this.

The corporate governance framework should be complemented by an effective, efficient solvency framework and by effective enforcement of creditor rights.

1.2 Stakeholder Theory:

An application of the agency theory provides insights into theoretical practices in the accounting and financial areas, while the stakeholder theory describes unethical practices that affect the employees, investors, creditors, government agencies, competition and the public at large in the case of Enron.

The stakeholder management and effective corporate performance are related; in fact a specific branch of stakeholder literature that links corporate practices and firm performance is used "instrumental stakeholder theory".

The extent of participation of other stakeholders has been on the increase and therefore, need to be taken into account. However, the arguments against the stakeholder theory are: diversity of stakeholder’s ambiguity in expectations of the stakeholders, complexity of trade-offs balancing stakeholder interests, and difficulties in verifying and measuring values to stakeholders.

2.3 Stakeholders’ Value Enhancement

The corporate governance philosophy is based on the premise that active participation by stakeholders in governance adds significant value to the process of wealth creation. The principles of the corporate governance as required by clause 49, stipulates the parameters of accountability, control and reporting functions of the board of directors and encompass the relationship among various participants in shaping the direction and performance of the corporation. It also calls for establishing a proper and a viable relationship amongst the various participants of a corporation, the board, management team, shareholders and other stakeholders. Corporate governance has shifted their focus to a broader beneficiary category known as stakeholders which also includes employees and ex-employees, vendor, business partners, customers, clients, regulators, society etc.

According to OECD principles of corporate governance "a sincere discharge of true accountability towards stakeholders would lead to achieve corporate wealth maximization, estors’ confidence, corporate image building and enhanced market capitalization. This can be achieved with clear and transparent management system and integral philosophy of maximizing wealth."


In this regard the Report of National Associations of Corporate Directors NACD, New York states that, “Corporate Governance ensures that long term strategic objectives and plans are established and that the proper management structure (Organization, systems and people) is in place to achieve those objectives, while at the same time making sure that the structure functions to maintain the corporation integrity reputation, responsibility to its various constituencies”. Therefore, it becomes imperative that there should be proper dissemination of information to enhance the stakeholder’s confidence in the corporate sector, by providing a fairly good idea and working culture, financial and commercial functioning, environment and the direction of the companies.

4.4 Definitions of Stakeholders

Stakeholders are interested in the successful growth of the company as their own interests are aligned with the company. All the stakeholders can be broadly grouped under five categories:

A. Employees
B. Creditors
C. Consumers
D. Society
E. Government

The common ground for satisfaction of the stakeholder is a under:

- Transparency
- Accountability
- Fairness
- Responsibility

Employees:

Human resource when managed properly has the capacity to bestow significant competitive advantage to companies. Well-managed human resources have the capacity to think, innovate and solve problems. Dissatisfaction of employees may result in underproduction or alienated workforce. The company shall have policies to enhance performance of employees
through Performance enhancing mechanisms, such as adequate pay and incentives, work satisfaction, and appropriate training. Managers today are dependent on educated employees to produce innovative, high-quality work, therefore a development and retention policy shall be in practice.

Employee participation in corporate governance systems can be found in many countries and corporations throughout the world. It includes rights to consultation, rights to nominate/vote for representative director, Compensation/privatization programs making employees shareholders. The role of employees in corporate governance, for example, employee representatives on the board shall be disclosed to the company's shareholders. Internal whistle blowing allows the enterprise to take appropriate corrective actions before the misconduct becomes a public issue. It should therefore be assisted by putting in place confidential reporting mechanisms that protect employees against any potential retribution.

**Creditors:**

OECD principle “The corporate governance framework should be complemented by an effective, efficient insolvency framework and by effective enforcement of creditor rights”.

Editor's value enhancement refers to effective insolvency framework and debt servicing. The creditor rights most essential for debt finance are those to repossess collateral and to have a say in reorganization. Alliances with suppliers and other business partners are now a competitive advantage as corporate relations with other stakeholders such as creditors; suppliers can either seize opportunities to achieve superior performance, or may pose potential risks if mismanaged. In some countries, the law makes it difficult for lenders to repossess collateral in part because such repossession can lead to the liquidation of firms, which is viewed as socially undesirable. In these countries, lenders may still have some powers against borrowers through their votes in decisions on how to reorganize the company and pay off the creditors.

**Consumers**

A customer also known as a client, buyer, or purchaser is the recipient of a good, service, product, or idea, obtained from a seller, vendor, or supplier for a monetary or other valuable
consideration. Customers are generally categorized into two types: An intermediate customer or trade customer who is a dealer that purchases goods for re-sale.

Enhancement of consumer value refers to access to sufficient information makes the consumers more comfortable and satisfied with the products and services. The satisfaction of consumers results in continuous patronage and brand loyalty. The corporate sector has realized the importance of understanding the customers need for survival in the competitive market.

D. Society:

Enhancement of value for this stakeholder refers to effectiveness of social welfare projects. All the efforts and activities in any economy shall result in betterment in the standard of living of the people. It is the responsibility of business enterprises to implement effective social welfare projects to take care of the people and the planet - protection of environment. This helps to assure that corporations operate for the benefit of society as a whole. Companies increasingly disclose their environmental and social policies, and performance. These disclosures range from brief philosophical statements to in-depth disclosures of policies, goals and performance, particularly common in companies with large environmental and social impacts such as energy extraction or mining, but relevant to virtually any company. Socially responsible investing as well as corporate social responsibility attract major attention of not only investors but also stakeholders nowadays can be both challenging, risky but also rewarding when regarding Social indexes like the FTSE4GOOD or the Dow Jones Sustainability Worlds Indexes.

E. Government:

The regulatory frame work of corporate governance in India consists of the companies legislation, SEBI Act 1992, the Securities Contract Act 1956, the listing agreement etc. The Companies Act 1956 has far reaching implications that significantly governs the corporate management in India. The companies Act was subsequently amended many times to plug the oopholes observed in practice. Securities and Exchange Board of India (SEBI) has brought in some amendments in listing agreement to make corporate governance mandatory. Clause 24A requires compliance with SEBI guidelines on disclosure and investor protection, Clause 40A
als with substantial acquisition of shares and takeover of listing agreement. Clause 43 requires disclosure of delisting and the reason thereof; Clause 45 deals will public offer to issue shares, Clause 46, requires the company to appoint company secretary who shall act as compliance officer. Clause 49, revision 2004, states that all the companies having paid up share capital of Rs. 3 crores and above or net worth of Rs. 25 crores or more at any time in the history the company shall comply with the mandatory requirements. Ministry of Company affairs requires the filing of reports in time and recently by e-filing procedure.

3.5 Corporate Social Responsibility:

Mechanisms protecting the rights of other stakeholders like suppliers; dealers; customers; editors; joint venture partners; banks; and employees become more and more important innes of advanced corporate social responsibility (OECD Principle IV). Stakeholders can be protected by a variety of means including the law, individual contracts, and codes of best practices.

3.6 Conflict of Interest:

There is conflicting interest among the shareholders and different stakeholders who make conflicting claims on the company. For example, the expectations of the shareholders may clash with those of the employees, particularly when there is need for companies to lower costs in der to sustain in the competition and retain the bottom line for payment of continued dividends, which ultimately may lead to severe ‘downsizing’ and ‘loss of jobs’. Many more examples may cited. However, these conflicting claims demonstrate that not all stakeholders are equal and their relative power may change with events. Stakeholders interact within a system, which is ever-widening boundaries, due to complexity and globalization.

3.7 Summary:

Corporate governance is not simply a matter of giving investors more control over top management. To add value, the top management must consistently balance the demands of the

Subhash Chandra Das, 'Corporate Governance in India an Evaluation', Prentice Hall, New Delhi, (2008), p.61
Disciplines of four distinct markets-product markets (consumers), labour markets (specialized employees), the technology market (suppliers), and capital markets (investors).

It is increasingly agreed that responsible corporate behaviour can enhance the performance of the enterprise and reduce potential risks. It is important that boards consider not only the quality of a company’s relations with shareholders, but also its relations with other contributors of resources to the company, such as employees, creditors and suppliers.

**Transparency and Disclosure**

Transparency and disclosure of required information is essential for good governance. 

"Transparency is the heart of corporate governance. With the increasing demands on disclosure, companies cannot survive without putting in place internal control architecture that would enable timely disclosure without risking reputation." Dr. Madhav Mehra.

The Report of Kumar Mangalam Birla Committee on Corporate Governance emphasized the importance of corporate disclosure, “Strong Corporate Governance is indispensable to resilient and vibrant capital markets and is an important instrument of investor protection. It is the blood, which fills the veins of transparent corporate disclosure and high quality accounting practices. It is the muscle that gives a viable and accessible financial reporting structure”.

**1 Timely and Accurate Disclosure**

The Organization for Economic Cooperation and Development (OECD) indicated that the corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership and governance of the company.

A. Disclosure should include, but not be limited to, material information on:

1. The financial and operating results of the company.
2. Company objectives.

3. Major share ownership and voting rights.

4. Remuneration policy for members of the board and key executives, and information about board members, including their qualifications, the selection process, other company directorships and whether they are regarded as independent by the board.

5. Related party transactions.

6. Foreseeable risk factors.

7. Issues regarding employees and other stakeholders.

8. Governance structures and policies, in particular, the content of any corporate governance code or policy and the process by which it is implemented.

B. Information should be prepared and disclosed in accordance with high quality standards of accounting and financial and non-financial disclosure.

C. An annual audit should be conducted by an independent, competent and qualified auditor in order to provide an external and objective assurance to the board and shareholders that the financial statements fairly represent the financial position and performance of the company in all material respects.

D. External auditors should be accountable to the shareholders and owe a duty to the company to exercise due professional care in the conduct of the audit.

E. Channels for disseminating information should provide for equal, timely and cost efficient access to relevant information by users.

F. The corporate governance framework should be complemented by an effective approach that addresses and promotes the provision of analysis or advice by analysts, brokers, rating agencies and others, that are relevant to decisions by investors, free from material conflicts of interest that might compromise the integrity of their analysis or advice.
2. Disclosures required under Clause 49

Basis of related party transactions

1. A statement in summary form of transactions with related parties in the ordinary course of business shall be placed periodically before the audit committee.

2. Details of material individual transactions with related parties which are not in the normal course of business shall be placed before the audit committee.

3. Details of material individual transactions with related parties or others, which are not at an arm’s length basis, should be placed before the audit committee, together with Management’s justification for the same.

Disclosure of Accounting Treatment

Where in the preparation of financial statements, a treatment different from that described in an Accounting Standard has been followed, the fact shall be disclosed in the financial statements, together with the management’s explanation as to why it believes such alternative treatment is more representative of the true and fair view of the underlying transaction in the Corporate Governance Report.

Board Disclosures – Risk management

The company shall lay down procedures to inform Board members about the risk assessment and minimization procedures. These procedures shall be periodically reviewed to ensure that executive management controls risk through means of a properly defined framework.

Proceeds from public issues, rights issues, preferential issues etc.

When money is raised through an issue (public issues, rights issues, preferential issues etc.), it shall disclose to the Audit Committee, the uses/applications of funds by major category (capital expenditure, sales and marketing, working capital, etc), on a quarterly basis as a part of their quarterly declaration of financial results. Further, on an annual basis, the company shall prepare

Revised Clause 49 SEBI Listing agreement. 2004
ement of funds utilized for purposes other than those stated in the offer document / 
rectus / notice and place it before the audit committee. Such disclosure shall be made only 
each time that the full money raised through the issue has been fully spent. This statement 
be certified by the statutory auditors of the company. The audit committee shall make 
riate recommendations to the Board to take up steps in this matter.

muneration of Directors

All pecuniary relationship or transactions of the non-executive directors vis-à-vis the 
company shall be disclosed in the Annual Report.

Further the following disclosures on the remuneration of directors shall be made in the 
section on the corporate governance of the Annual Report:

a. All elements of remuneration package of individual directors summarized under 
    major groups, such as salary, benefits, bonus, stock options, pension etc.

b. Details of fixed component and performance linked incentives, along with the 
    performance criteria.

c. Service contracts, notice period, severance fees.

d. Stock option details, if any – and whether issued at a discount as well as the period 
    over which accrued and over which exercisable.

The company shall publish its criteria of making payments to non-executive directors in 
its annual report. Alternatively, this may be put up on the company’s website and 
reference drawn thereto in the annual report.

The company shall disclose the number of shares and convertible instruments held by 
non-executive directors in the annual report.

Non-executive directors shall be required to disclose their shareholding (both own or held 
by / for other persons on a beneficial basis) in the listed company in which they are
proposed to be appointed as directors, prior to their appointment. These details should be disclosed in the notice to the general meeting called for appointment of such director.

Management Discussion and Analysis

Management Discussion and Analysis report should form part of the Annual Report to the shareholders, which should include discussion on the following matters within the limits set by the company’s competitive position:

i. Industry structure and developments.
ii. Opportunities and Threats.
iii. Segment-wise or product-wise performance.
iv. Outlook
v. Risks and concerns.
vi. Internal control systems and their adequacy.
vii. Discussion on financial performance with respect to operational performance.
viii. Material developments in Human Resources / Industrial Relations front, including number of people employed.

Senior management shall make disclosures to the board relating to all material financial and commercial transactions, where they have personal interest, that may have a potential conflict with the interest of the company at large (for e.g. dealing in company shares, commercial dealings with bodies, which have shareholding of management and their relatives etc.) The term "senior management" shall mean personnel of the company who are members of its core management team excluding the Board of Directors. This would also include all members of management one level below the executive directors including all functional heads.

Information to Shareholders

In case of the appointment of a new director or re-appointment of a director the shareholders must be provided with the following information:

A brief resume of the director;
b. Nature of his expertise in specific functional areas;

c. Names of companies in which the person also holds the directorship and the membership of Committees of the Board; and

d. Shareholding of non-executive directors as stated in Clause 49 (IV) (E) (v) above

Quarterly results and presentations made by the company to analysts shall be put on company’s web-site, or shall be sent in such a form so as to enable the stock exchange on which the company is listed to put it on its own web-site.

A board committee under the chairmanship of a non-executive director shall be formed to specifically look into the redressal of shareholder and investors complaints like transfer of shares, non-receipt of balance sheet, non-receipt of declared dividends etc. This Committee shall be designated as ‘Shareholders/Investors Grievance Committee’.

To expedite the process of share transfers, the Board of the company shall delegate the power of share transfer to an officer or a committee or to the registrar and share transfer agents. The delegated authority shall attend to share transfer formalities at least once in a fortnight.

4.3 Voluntary Disclosure and Regulatory Frameworks

Disclosure is often determined by national regulations, international standards and guidelines. The regulatory framework provides recommendations and requirements about what and how to disclose. However, even where no legislation exists, it is considered good practice for companies to disclose additional information, so that stakeholders are provided with all relevant information in order to assess a company’s performance according to their interests.

Transparency and disclosure of quality information is an important aspect of Good Corporate Governance. The better there is transparent disclosures the better is the performance of the company to the satisfaction of all the stakeholders.
Performance of the company

The objective of the study is to analyze the performance of the companies in two parts, performance in view of compliance with Government and regulatory agencies and the second in terms of financial results.

Under all Compliance: The Ministry of Corporate Affairs has been working towards strengthening of the corporate governance framework through a two pronged strategy. Some aspects which needed to be incorporated in the law have been included in the Companies Bill, 1999 now under examination by Parliament. However, keeping in view the objective of encouraging the use of better practices through voluntary adoption, the Ministry has decided to lift a set of voluntary guidelines which not only serve as a benchmark for the corporate sector but also help them in achieving the highest standard of corporate governance. These guidelines provide for a set of good practices which may be voluntarily adopted by the Public companies. Private companies, particularly the bigger ones, may also like to adopt these guidelines. The guidelines are not intended to be a substitute for or addition to the existing laws but is commendatory in nature.

1. CORPORATE GOVERNANCE VOLUNTARY GUIDELINES 2009

There are different practices in different countries of the world and it has been universally accepted that there cannot be one global system of corporate governance for the whole world. The Ministry of Company affairs has presented to the corporate sector of India to adopt the voluntary guidelines which includes all the principles, codes, rules and regulations for successful practice of Corporate Governance.

The Voluntary Guidelines consists of six categories which are discussed as under;

1. Board of Directors
2. Responsibilities of the Board
3. Audit committee of Board

Published by Ministry of Corporate Affairs, Government of India, New Delhi, (2009).
4. Auditors
5. Secretarial Audit
6. Institution of Mechanism for Whistle Blowing

**Board of Directors**

Under this there are three sub-headings which deal with:

- **Appointment of Directors:** This section gives the detailed procedure for appointments to the Board, separation of offices of chairman & chief executive officer, constitution and functions of nomination committee comprising of majority of Independent Directors, including its Chairman, and restricts the number of companies in which an individual can serve as a Non-Executive Director or Independent Director as seven in the case of a Managing Director or Whole-time Director in a public company.

- **Independent Directors:** This section explains the ‘Attributes for Independent Directors’ and insist the production of Certificate of Independence. Tenure for Independent Director is fixed as six years and restricted to a maximum of three tenures and the number of companies in which he can act as independent director is restricted to seven. Independent Directors shall have the Option and Freedom to meet Company Management periodically.

- **Remuneration of Directors:** Remuneration policy shall ensure that the level and composition of remuneration is reasonable and sufficient to attract, retain and motivate directors of the quality required to run the company successfully. There shall be Guiding Principles-Linking Corporate and Individual Performance. This section give details of Remuneration of Non-Executive Directors (NEDs), Structure of Compensation to NEDs, Remuneration of Independent Directors (IDs), and constitution of Remuneration Committee with at least three members, majority of whom should be non executive directors with at least one being an Independent Director.

**Responsibilities of the Board**

This section details the responsibility of Board in respect of the following important matters have been clearly stated. A summary is presented as under;
Training of Directors: Ensure that directors are inducted through a suitable familiarization process covering, inter-alia, their roles, responsibilities and liabilities.

Enabling Quality Decision Making: Ensure that there are systems, procedures and resources able to ensure that every Director is supplied, in a timely manner, with precise and concise information in a form and of a quality appropriate to effectively enable/discharge his duties.

Risk Management: The Board, its Audit Committee and its executive management should actively identify the risks impacting the company's business and document their process of identification, risk minimization, risk optimization as a part of a risk management policy or strategy.

Evaluation of Performance of Board of Directors, Committees thereof and of Individual Directors: The Board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors.

Board to place Systems to ensure Compliance with Laws: To safeguard shareholders' interest and the company's assets, the Board should, at least annually, conduct a review of the effectiveness of the company's system of internal controls.

Audit Committee of Board

Constitution of Audit Committee: There should be at least a three-member Audit Committee, with Independent Directors constituting the majority. The Chairman of such committee should be an Independent Director. All the members of audit committee should have knowledge of financial management, audit or accounts.

Powers Audit Committee: Audit Committee shall have access to information contained in records of the company; and obtain professional advice from external sources. The Audit Committee should also have the facility of separate discussions with both internal and external auditors as well as the management.
Role and Responsibilities of Audit Committee: The Audit Committee should have the responsibility to monitor the integrity of the financial statements of the company; review the company's internal financial controls, internal audit function and risk management systems; make recommendations in relation to the appointment, reappointment and removal of the internal auditor and to approve the remuneration and terms of engagement of the external auditor; review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process.

Auditors

Appointment of Auditors: Audit Committee of the Board should be the first point of reference regarding the appointment of auditors. It should check the profile of the audit firm, qualifications and experience of audit partners, strengths and weaknesses, if any, of the audit firm and other related aspects.

Certificate of Independence: Every company shall obtain a certificate from the auditor certifying his independence and arm's length relationship with the client company. The certificate of Independence should certify that the auditor together with its consulting and specialized services affiliates, subsidiaries and associated companies or network or group entities has not/have not undertaken any prohibited non-audit assignments for the company and are dependent vis-à-vis the client company.

Rotation of Audit Partners and Firms: the company may adopt a policy of rotation of auditors which may be as under:

Audit partner - to be rotated once every three years
Audit firm - to be rotated once every five years.

A cooling off period of three years should elapse before a partner can resume the same audit assignment. This period should be five years for the firm.

Need for clarity on information to be sought by auditor and/or provided by the company: There should be clarity between company management and auditors on the nature and amount of information and frequency for supply/obtaining such information.
Appointment of Internal Auditor: To ensure the independence and credibility of the internal audit process, the Board may appoint an internal auditor and such auditor, where appointed, should not be an employee of the company.

Secretarial Audit

The Board has responsibility of ensuring transparent, ethical and responsible governance of the company. It is important that the Board system and compliance mechanisms of the company are robust. To ensure this, the companies may get the Secretarial Audit conducted by a competent professional. The Board should give its comments on the Secretarial Audit in its report to the shareholders.

Institution of Mechanism for Whistle Blowing

The companies should ensure the institution of a mechanism for employees to report concerns about unethical behaviour, actual or suspected fraud, or violation of the company's code conduct or ethics policy. The companies should also provide for adequate safeguards against victimization of employees who avail of the mechanism, and also allow direct access to the chairperson of the Audit Committee in exceptional cases.

1.2 Financial Analysis:

Corporate Governance is a dynamic method to channelize the national savings to the productive users for enhancement of value. The corporate sector is a trusted vehicle for the sustainable wealth creation in any economy. Corporate Governance practices shall make every business entity responsible and accountable for every rupee invested by the investors and shall strive and succeed value addition. A small lapse in respect of corporate governance on the part of a company will pull down the market value of its share below the real value and wean away investors.

Profit after Tax:

Profit after Tax (PAT) is the net profit earned by the company after deducting all expenses like interest, depreciation and tax. PAT can be fully retained by a company to be used
the business. Dividends, if declared, are paid to the share holders from this residue. The net amount earned by a business after all taxation related expenses have been deducted. The profit after tax is often a better assessment of what a business is really earning and hence can use in its calculations rather than its total revenues. The Net Profit of the establishment discloses the actual result the business in terms of money value. This is the basic criterion which openly shows the financial performance of the company.

**Economic Value Addition (EVA):**

Effectiveness of Corporate Governance is measured in financial terms as quantum of ‘wealth creation’ or Economic Value Addition (EVA). Economic Value Added (EVA) is important because it is used as an indicator of how profitable company projects are and it therefore serves as a reflection of management performance.

The idea behind EVA is that businesses are only truly profitable when they create wealth for their shareholders, and the measure of this goes beyond calculating net income. Economic value added asserts that businesses should create returns at a rate above their cost of capital. The economic value calculation has many advantages. It summarizes how much and where a company created wealth. It includes the balance sheet in the calculation and encourages managers to think about assets as well as expenses in their decisions.

The EVA calculation depends heavily on invested capital, and it is therefore most applicable to asset-intensive companies that are generally stable. Thus, EVA is more useful for manufacturers, for example, than software companies or service companies with a lot of tangible assets. Economic value added (EVA) is also referred to as economic profit.

The formula for EVA is:

\[
\text{EVA} = \text{Net Operating Profit after Tax} - (\text{Capital Invested} \times \text{WACC})
\]

shown in the formula, there are three components necessary to solve EVA:

1. Net Operating Profit after Tax (NOPAT),
2. Invested capital, and
3. The Weighted Average Cost of Capital (WACC)
Net Operating Profit after Taxes (NOPAT) can be easily found on the corporation's income statement. The next component, capital invested, is the amount of money used to fund a particular project. The weighted-average cost of capital (WACC) has to be calculated if the formation is not provided. The idea behind multiplying WACC and capital investment is to assess a charge for using the invested capital. This charge is the amount that investors as a group need to make their investment worthwhile.

**Tobin's 'q' Theory and Definition**

Good practices of Corporate Governance will enhance the earning capacity of a firm. This value addition can be ascertained by calculating Tobin’s q, where ‘q’ represents the ratio of the market value of a firm's existing shares (share capital) to the replacement cost of the firm's physical assets (thus, replacement cost of the share capital). Economics theory of investment behavior states that if q (representing equilibrium) is greater than one (q > 1), additional investment in the firm would make sense because the profits generated would exceed the cost of firm's assets. If q is less than one (q < 1), the firm would be better off selling its assets instead of trying to put them to use. The ideal state is where q is approximately equal to one denoting that the firm is in equilibrium. Also called general equilibrium theory or 'q' theory, it was proposed by the US Nobel laureate economist James Tobin.

Tobin’s q was introduced in 1968 by James Tobin and William Brainard. Tobin's q is the ratio between the market value and replacement value of the same physical asset. Use of the letter "q" however, did not appear until Tobin's 1969 article. "A general equilibrium approach to monetary theory".

Tobin (1969) writes: One, the numerator, is the market valuation: the going price in the market for exchanging existing assets. The other, the denominator, is the replacement or production cost: the price in the market for the newly produced commodities. We believe that this ratio has considerable macroeconomic significance and usefulness, as the nexus between financial markets and markets for goods and services.

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The formula is: \[ q = \frac{\text{Market value of installed capital}}{\text{Replacement cost of capital}} \]

Tobin's q measures two variables; the current price of capital assets as measured by accountants and the market value of equity and bonds, but there are other elements that may affect the value of q, namely:

- Market hype and speculation, reflecting, for example, analysts' views of the prospects for companies, or speculation such as bid rumors.

- The "intellectual capital" of corporations, that is, the unmeasured contribution of knowledge, goodwill, technology and other intangible assets that a company may have but aren't recorded by accountants. Some companies seek to develop ways to measure intangible assets such as intellectual capital.

Tobin's q is said to be influenced by market hype and intangible assets so that we see swings in q around the value of 1. If the market value reflected solely the recorded assets of a company, Tobin's q would be 1.0.

If Tobin's q is greater than 1.0, then the market value is greater than the value of the company's recorded assets. This suggests that the market value reflects some unmeasured or recorded assets of the company. High Tobin's q values encourage companies to invest more in total because they are "worth" more than the price they paid for them.

Summary:

In this chapter all the theoretical literature on corporate governance has been discussed and the actual implementation of this theory will be discussed and analyzed in the next Chapter 3 analysis of Secondary information. The level of implementation and compliance has been assessed by awarding points for compliance.