“Over the last decade or so, Corporate Governance has come to acquire an increasingly important place in the conduct of the corporate sector globally. This is understandable considering the expanded role of the corporate sector not just in creating wealth but even in many societal issues, all of which necessitates that society places a higher degree of trust in the same corporates. Thus we have seen several bodies, internationally and nationally engage with the issue of what comprises good Corporate Governance and through the efforts of these bodies, we now have a rich and growing body of the do’s and don’ts on the issue.”

– Ratan N. Tata, Chairman, Tata Group.
Different countries’ economics are organized in very different ways, decisions about how capital is allocated is different and this is the very reason different countries have different paths to follow the corporate governance. The history of adapting the path to follow and implement corporate governance in different countries like, The United States, The United Kingdom, Germany, Japan, China and India are different.

2.1 History of Corporate Governance across the World

2.1.1 United States of America (USA):
In 1930’s, a remarkable democratization of shareholding took place between the period of World War I and the end of World War II. The benefits of democratization and diversification depend on the depth of the stock market. Popular magazines on share ownership, and popular media coverage of Wall-Street celebrities brought Middle American wealth into the stock market, vastly deepening it and thus making the sacrifice of diversification for control more attractive than elsewhere.

America’s response to the Great Depression then razed much of what family capitalism remained. Two great pyramids, the Insull and Van Sweringen business groups, collapsed after the 1929 crash. These high profile collapses appear to have linked to the Depression with highly concentrated corporate control in the public mind, justifying a barrage of progressive reforms. A series of regulatory reforms governing banks, insurance companies, mutual funds and pension funds prevented any of these organizations from accumulating any serious corporate governance influence as per 1937 data on block holding in the top listed 200 US firms.

Although the hostile takeovers of the 1980s disrupted this arrangement for some forms, and some United States institutional investors were clearing their throats, this situation has kept most American firms freestanding and
professionally run ever since. Since then, corporate governance has been implemented in most of the companies.

2.1.2 United Kingdom (UK):
Comparison of the firms founded in 1900 to another founded in 1960 has been done in one of the studies conducted. (Monks & Minow, 2008) It is found that ownership grows diffuse in both sets of firms at roughly the same rate. Based on this, an argument is made that the forces that made founding families withdraw from corporate governance in the modern United Kingdom also operated a century ago. Adding to this, a discussion concludes that shareholder rights in the United Kingdom were extremely weak until the later part of the 20th century, and shareholder legal protection permits diffuse ownership in the UK.

Providing a descriptive summary of UK corporate governance in greater generality, the pyramids gained importance at the middle of the century. The corporate disclosure, implemented in 1948, made hostile takeovers less risky for raiders, and that pyramids developed as a defense against hostile takeovers. However, they propose that British corporate insiders were and are governed by higher standards of ethical conduct, which preclude the extraction of such private benefits. Given this, British corporate insiders were more readily convinced to sell their control blocks and dismantle their pyramids. Thus, the current diffuse ownership of British corporations came to prevail early in the 20th century and still persists.

2.1.3 Germany:
Fohlin (2004) argues that Germany’s large universal banks were less important to its history of corporate governance than is commonly believed. German industrialization advanced rapidly in the late 19th century, financed by wealthy merchant families, foreign investors, small shareholders and private banks, industrial firms with bankers on their boards did not perform better than other firms.
German corporate governance appears to be thoughtfully developed in this era. The company law of 1870 created the current dual board structure to protect small shareholders and public from self-serving insiders. It also required uniformity and consistency in accounting, reporting and governance.

The modern German economy thus consists primarily of family controlled pyramidal groups and nominally widely held firms that are actually controlled by the top few banks via proxies. The leading banks collectively also control dominant blocks of own shares. In more recent times, the advantages available to German companies have become ‘disadvantages’ as they have not been able to attract capital from Institutional Investors in global markets, due to ‘parochial governance practices that have obstructed share holders rights’. (Monks and Minow (2001))

2.1.4 Japan:
The history of corporate governance in Japan is more complicated and variegated than in any other major country. Prior to 1868, Japan was a deeply conservative and isolationist country. Business families were at the bottom of a hereditary caste system – beneath priests, warriors, peasants, and craftsmen. Unsurprisingly, this moral inversion led to stagnation. Yet the necessity of running a densely populous country forced Japan’s feudal shoguns to give prominent mercantile families, like the Mistui and Sumitomo, steadily a greater influence. Japan fell traditionally into the insider-dominated groups and had a ‘credit-based financial system (Zysman, 1983) as the economy was characterized by inter company shareholdings, inter company directorships and frequently substantial bank involvement.

Recently, the trend has been toward a more market- dominated Japanese system of corporate governance. (Cooke and Sawa, 1998)

These groups, called zaibatsu, were family controlled pyramids of listed corporations, much like those found elsewhere in the world. Later, other
groups like Nissan, a pyramidal business group with a widely held firm at its apex, joined in as Japan’s economy roared into the 20th century. Thus Japan began its industrialization with a mixture of family and state capitalism. Shareholders eagerly bought shares, especially in numerous subsidiaries floated by these great business groups.

2.1.5 China:
Chinese corporate governance in the late 19th and early 20th centuries is of interest because it corresponds to the beginning of china’s industrialization and sees the attempted transplanting of western institutions into a nonwestern economy. Pre-communist China’s industrial development may thus offer more interesting lessons for modern emerging economies than does post-communist China herself, pre-revolutionary capitalism also provides a model of “a market economy with Chinese characteristics.”

Portfolio investors, unable to influence corporate governance after this fact, stayed out of stocks. This kept the Chinese stock market illiquid and subject to severe boom and bust cycles. This, in turn, kept insiders from selling out and diversifying, underscoring the value of their private benefits of control.

2.1.6 India:
The fundamentals of Corporate Governance have its deep roots in Indian History. But surprisingly it is very less known to us. Our own ancient texts have laid down sound principles of governance which seem very relevant to modern day corporate requirements.

Years back in 1600, The East India Company was arguably the first to be chartered as a Company by the then Queen Elizabeth I, with a monopoly of trade between England and Far East. Since then, corporations have come a long way, both in terms of their power and wealth-creating potentials, and of institutionalized checks and balances to ensure their sound operations within their mandates and transparent reporting back to the shareholders.
Since then the Corporate Governance has become the crucial issue in the Corporate World. Different countries across the World follow different Corporate Governance Systems. India also follows more or less the UK Model of Corporate Governance.

### 2.2 Models of Corporate Governance

- The Board of Directors seldom appears on the management organization chart yet it is the ultimate decision making body in a Company. The role of management is to run the enterprise while the role of the board is to see that it is being run well and that too in the right direction.

- A useful way of depicting the interaction between management and the board is to present the board as a circle superimposed on the hierarchical triangle of management. This model can be applied to the governance of any corporate entity, private or public, profit oriented or service based organization. The circle and Triangle model is a powerful analytical tool. (A.C. Fernando (2009))

- Corporate Governance System varies around the World. Scholars tend to suggest three broad versions:
  - The Anglo-American Model;
  - The German Model;
  - The Japanese Model.
2.2.1 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. The major features of the Anglo-American or Anglo-saxon model of the corporate governance are as follows:

- The ownership of companies is more or less equally divided between individual shareholders and institutional shareholders.
- Directors are rarely independent of management.
- Companies are typically run by professional managers who have negligible ownership stakes. There is a fairly clear separation of ownership and management.
- Most institutional investors are reluctant for certain activities. They view themselves as portfolio investors interested in investing in a broadly diversified portfolio of liquid securities. If they are not satisfied with a
company’s performance, they simply sell the securities in the market and quit.

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

### 2.2.2 The German Model

It is also known as **two-tier board model**. Corporate governance in the German model is exercised through two boards, in which the upper board supervises the executive board on behalf of stakeholders and is typically societal-oriented. In this model, although shareholders own the company, they do not entirely dictate the governance mechanism. They elect 50 percent of members of supervisory board and the other half is appointed by labor unions ensuring that employees and laborers also enjoy a share in the governance. The supervisory board appoints and monitors the management board.
This is the 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 reality of power in the enterprise lies in the relationships between top management in the companies in the keiretsu network. The approach bears some comparison with Korean chaebol. 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.
2.2.4 Indian Corporate Governance Model

The Indian companies are governed by the Company’s Act of 1956 which follows more or less the UK model. The pattern of private companies is mostly that of closely held or dominated by a founder, his family and associates. India has adopted the key tenants of the Anglo-American external and internal control mechanism after economic liberalization.

The structure and processes of corporate governance are not universally same in all countries. Different countries have adopted different structure and processes in governing their companies depending on suitability of their socio-culture, economic environment, government policy, capital and money market systems etc. Whatever structures of corporate governance are adopted, one thing is common that the board of directors has been reorganized as the heart of the structure of corporate governance and the board processes have been accepted.
as the most important processes of governance. It has also been reorganized that along with the board of directors, the other participants, viz. shareholders including institutional investors or large shareholders, other stakeholders, banks and auditors etc. do have significant roles in the governance structures and their commitments in the processes of corporate governance. Therefore, while discussing the various structures and processes of corporate governance, it will be prudent to touch upon the roles and commitments of these participants simultaneously, without which the discussion on governance structures and processes remains incomplete. (Vasudha Joshi (2004), Jayanti and Subrate Sarkar, (September 2000))

2.2.5 Comparative study of international corporate governance practices:

<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>Features</th>
<th>Anglo-American Corporate Governance</th>
<th>German Corporate Governance</th>
<th>Japanese Corporate Governance</th>
<th>Indian Corporate Governance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Corporate objective</td>
<td>Shareholder value</td>
<td>Long-term corporate value</td>
<td>Long-term corporate value</td>
<td>Shareholder value</td>
</tr>
<tr>
<td>4.</td>
<td>Measure of Success</td>
<td>Return on financial capital</td>
<td>Return on human capital</td>
<td>Return on social capital</td>
<td>Return on financial capital</td>
</tr>
<tr>
<td>5.</td>
<td>Decision-making</td>
<td>Checks and balances between voice and exit options. Outside stakeholders excluded.</td>
<td>Within the network of stakeholders including employees, local community.</td>
<td>Within the network includes business associates and banks as shareholders.</td>
<td>Management, outside stakeholders excluded.</td>
</tr>
<tr>
<td>6.</td>
<td>Control of corporates</td>
<td>Separated from ownership</td>
<td>Linked with ownership.</td>
<td>Linked with ownership.</td>
<td>Linked with ownership.</td>
</tr>
<tr>
<td>7.</td>
<td>Orientation</td>
<td>Short-term, driven by stock market prices.</td>
<td>Long-term</td>
<td>Long-term</td>
<td>Short-term gains</td>
</tr>
<tr>
<td>Sr. No.</td>
<td>Features</td>
<td>Anglo-American Corporate Governance</td>
<td>German Corporate Governance</td>
<td>Japanese Corporate Governance</td>
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<tr>
<td>9.</td>
<td>Capital Market (Primary)</td>
<td>Liquid</td>
<td>Less important, due to close ties with banks.</td>
<td>Less important, because to close ties with banks.</td>
<td>Less important due to institutional funding.</td>
</tr>
<tr>
<td>11.</td>
<td>Investor Commitment</td>
<td>Low</td>
<td>High, important in difficult times.</td>
<td>High, important in difficult times.</td>
<td>Low</td>
</tr>
<tr>
<td>12.</td>
<td>Major investors</td>
<td>Institutional shareholders; Individual shareholders; Business network; Employees; Government and Banks.</td>
<td>Banks; Business network; Employees; Government; Individual shareholders and Institutional Shareholders.</td>
<td>Business network; Main bank; Government; Institutional Shareholders, Individual Shareholders and Employees.</td>
<td>Directors and relatives, other Corporates; Foreign Investors; Govt. term lending Institutions; Public Shareholding; and Institutional Investors</td>
</tr>
<tr>
<td>15.</td>
<td>Board independence over management</td>
<td>Little</td>
<td>High</td>
<td>Little formality, more informality.</td>
<td>Little</td>
</tr>
<tr>
<td>16.</td>
<td>Executive Compensation</td>
<td>High</td>
<td>Moderate</td>
<td>Low</td>
<td>Moderate subject to govt. approval</td>
</tr>
<tr>
<td>17.</td>
<td>Dividend</td>
<td>High</td>
<td>Low</td>
<td>Low</td>
<td>Low, uncertain.</td>
</tr>
<tr>
<td>18.</td>
<td>Strength</td>
<td>Dynamic; market based; liquid capital; internationalization; non-problematic</td>
<td>Long-term industrial strategy; stable capital; Strong overseas investment; governance procedures.</td>
<td>Long-term industrial Strategy; stable capital.</td>
<td>Recent government and organizational activism (CII) towards corporate governance practices.</td>
</tr>
<tr>
<td>19.</td>
<td>Weakness</td>
<td>Instability; short-termism</td>
<td>Internationalization difficult; vulnerable to global capital market.</td>
<td></td>
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</tr>
</tbody>
</table>
2.3 Recommendations of Various International Committees on Corporate Governance

2.3.1 The Cadbury Committee:
In December 1992, the Cadbury Committee published the *Code of Best Practice* which recommended that boards of publicly-traded UK corporations include at least three outside directors and that the positions of the chairman of the board and chief executive officer not be held by a single individual. The underlying presumption was that these government-sponsored recommendations would lead to enhanced board oversight. As a test of presumption, corporate analyzes the relation between top management turnover and its performance. Corporate finds that CEO turnover increased following publications of the Code, that the relationship between CEO turnover and performance was strengthened following publication of the Code, and that the increase in the sensitivity of turnover to performance was concentrated among firms that adopted the Cadbury Committee’s recommendations. (Jay Dahya, John McConnell and Nickolaos Travlos, The Athens Laboratory of Business Administration, 2000)

The Cadbury Committee was appointed by the Conservative Government of the United Kingdom (UK) in May 1991 with a broad mandate to “address the financial aspects of corporate governance”. In December 1992, the Committee issued its report which recommended, among other things, that board of directors of publicly traded companies include at least three non-executive (i.e., outside) directors as members and that the positions of Chairman of the Board (Chairman) and Chief Executive Officer (CEO) of these companies be held by two different individuals. The apparent reasoning underlying the Committee’s recommendations is that greater independence of a corporate board will improve the quality of board oversight.

To appreciate the potential significance of the Cadbury Committee and its recommendations, it is important to appreciate the environment surrounding the establishment of the Committee. First, the Committee was appointed in the
aftermath of the “scandalous” collapse of several prominent UK companies during the later 1980s and early 1990s, including Ferranti International PLC, Colorol Group, Pollypeck International PLC, Bank of Credit and Commerce International (BCCI) and Maxwell Communication Corporation. The broadsheet press popularly attributed these failures and others to weak governance systems, lax board oversight, and the vesting of control in the hands of a single top executive. (Cadbury Committee Report, 1992)

2.3.2 The Greenbury Committee, 1995
This committee was set up in January, 1995 to identify the good practices by the Confederation of British Industry (CBI), in determining directors’ remuneration and to prepare a code of such practices for use by public limited companies of United Kingdom.

The Committee mainly focused on the following issues
- Accountability and level of Directors’ pay.
- Proper reporting to shareholders and greater transparency in the Process.

The Committee produced the Greenbury Code of Best Practice which was divided into following four sections:
- Remuneration Committee.
- Disclosures.
- Remuneration policy.
- Service Contracts and compensation.
(Greenbury Committee Report (1994), investigating board members’ remuneration and responsibilities)

2.3.3 The Hampel Committee, 1995
The Hampel Committee was set up in November, 1995 to promote high standards of corporate governance both to protect investors and to preserve and enhance the standing of companies listed on the London Stock Exchange.
The committee further developed the Cadbury Committee Report and recommended that:

- The auditors should report on internal control privately.
- The directors maintain and review all controls.
- Companies that do not already have an Internal Audit Function should from time to time review their need for one.

The Committee also introduced the Combined Code that consolidated the recommendation of earlier corporate governance. (Cadbury and Greenbury).

(The Hample Committee Report 1998)

2.3.4 The Combined Code, 1998

The Combined Code was subsequently derived from Ron Hampel Committee’s Final Report, Cadbury and the Greenbury Report.

- The stipulations contained in the Combined Code require, among the other things, that the Board should maintain a sound system of internal control to safeguard shareholders’ investment and the Companies’ assets.
- It was observed by this committee that the one common denominator behind the past failures in the corporate world was the lack of effective risk management.

2.3.5 The Turbnell Committee, 1999

The Tur nell Committee was set up by The Institute of Chartered Accountant in England and Wales (ICAEW) in 1999 to provide guidance to assist companies in implementing the requirements of the Combined Code relating to internal control.

- The Committee recommended that where companies do not have any internal audit function; the board should consider the need for carrying out an internal audit function.
- The Committee also recommended that the board of directors should confirm the existence of procedures for evaluating and managing the key risks.
According to this Committee, Corporate Governance is not a static concept, in fact it is dynamic, and thus needs to alter with the changes that occur in a business environment.

(The Turnbull Committee Report 1998)

2.3.6 Sarbanes-Oxley Act, 2002

Sarbanes-Oxley Act is one which codifies certain standards of good governance as specific requirement.

- The Act calls for protection to those who have the courage to bring frauds to the attention of the authority that has to handle frauds.
- The Sarbanes-Oxley Act (SOX ACT), 2002 is a sincere attempt to address all the issues associated with corporate failures to achieve quality governance and to restore investors’ confidence.
- The Act was formulated to protect investors by improving the accuracy and reliability of corporate disclosures, made precious to the securities laws and for other purposes. The Act contains a number of provisions that dramatically change the reporting and corporate director’s governance obligations of public companies, the directors and officers. (Cynthia A. Glassman, Commissioner, SEC)

2.4 Indian Committees and their Guidelines

Some major committees for corporate governance in India are:

- Kumar Manglam Birla Committee, 1999
- Naresh Chandra Committee Report, 2002
- Narayan Murthy Committee Report, 2003
- Dr. J. J Irani Committee on Company Law, 2005

2.4.1 Kumar Mangalam Birla Committee, 1999:

- The Birla Committee’s recommendations consists of mandatory recommendations, and non-mandatory recommendations.
- Mandatory recommendation includes composition of Board of director and audit committee, remuneration committee of the board procedure of board, management or manner of implementation.
- Non-mandatory recommendations includes role of the chairman, policy of remuneration committee, rights of shareholders, postal ballot procedure etc.

(The Chartered Secretary, March 2000)

2.4.2 Nareshchandra Committee Report, 2002
The Naresh Chandra Committee was appointed as a high-level committee to examine various corporate governance issues by the Department of Company Affairs on 21 August 2002. Naresh Chandra Committee report on ‘corporate Audit & Governance’ has taken forward the recommendations of the Kumar Mangalam Birla Committee on corporate governance which was set up by the Securities Exchange Board of India on the following counts:
- Representation of independent directors on a company’s board.
- The composition of the audit committee.

The Naresh Chandra Committee has laid down stringent guidelines defining the relationship between auditors and their clients. In a move that could impact small audit firms, the committee has recommended that along with its subsidiary, associates or affiliated entities, an audit firm should not derive more than 25 per cent of its business from a single corporate client.

The Committee has further recommended the following:
- Tightening of the noose around the auditors by asking them to make an array of disclosures.
- Calling upon CEOs and CFOs of all listing companies to certify their companies’ annual accounts, besides suggesting.
- Setting up of quality review boards by the Institute of Chartered Accountants of India (ICAI), Institute of Company Secretaries of India (ICSI) and Institute of Cost and Works Accountants of India, instead of a Public oversight board similar to the one in USA.
2.4.3 Narayana Murthy Committee Report, 2003
Under the committee on corporate governance set up by SEBI under N. R. Narayana Murthy, the terms of references were:

- to review the performance of corporate governance and
- to determine the role of companies in responding to rumor and other price sensitive information circulating in the market.

The committee report expresses its total concurrence with the recommendations contained in the Naresh Chandra Committee’s report on the following counts:

- Disclosure of contingent liability
- Certification by CEO’s and CFO’s
- Definition of independent directors
- Independence of Audit committees

The committee came out with two sets of recommendations namely, mandatory recommendation and non-mandatory recommendations.

Mandatory recommendation includes composition of audit committee, related party transactions, Proceeds from initials public offerings, risk management code of conduct for the Board or appointment of Nominee directors etc.

Non-mandatory recommendation pertains to moving to a regime providing for unqualified corporate financial statements, training of board members and evaluation of non-executive director’s performance by a peer group comprising the entire board of directors, excluding the director being evaluated.

2.4.4 Dr. J. J. Irani Committee Report on Company Law, 2005
The Government of India constituted an expert committee on Company Law on 2 December 2004, under the chairmanship of Dr. J. J. Irani. Set up to structurally evaluate the views of several stakeholders in the development of the Company Law in India in respect of the concept paper promulgated by the union ministry of company affairs, the J. J. Irani Committee has come out with suggestions that will go a long way in laying sound base for corporate growth in the coming
years. The main features of its recommendations pertaining to corporate governance are as follows:

- Number of Directors & their duration in company
- Age of Directors
- 1/3rd of Independent Directors (along with definition of Independent Director)
- Maximum No. of Directorship hold by Individual
- Remuneration Policy
- Sitting Fee Structure for Directors
- Requisite Board Meetings in a year
- Number of Independent Directors in Audit Committee
- Constitution of Remuneration Committee
- Protections of Minority shareholders rights
- Appointment of Auditors
- Certificate Issued by CEO & CFO
- Subsidiary Company Transactions
- Disclosure of directorship & shareholding pattern of the company
- Responsibility of the Board in Public Subscriptions
- Roles & Responsibilities of Independent Directors
- Appointment of Stakeholders Relationship Committee
- Appointment of Nominee Directors
- Interactive Dialogue between professional bodies and corporate sector to enable evolution of corporate governance codes
- Appointment of Regulators to monitor the end use of funds collected from the public
- Credit Rating Mechanism should be followed by corporate
- Whistle-blower concept

(Irani Committee Report on Company Law (2005))

It is important to mention here that despite various recommendations made by the above committees on corporate governance, the Committees kept silence on two major issues on corporate governance. They are:
- Chairman and CEO Duality (particularly in regard to separation of these two posts), and
- Appointment of Nomination Committee.

**2.5 Role of SEBI**

With the abolition of the office of the Controller of Capital Issues, The Security and Exchange Board of India (SEBI) was constituted. It was established originally in 1988 but was only given statutory power with enactment of the SEBI Act in January 1992. The SEBI did not obtain complete autonomy and authority to pursue its twin goals of investor protection and market development. The authority in key areas remained with the Department of Company Affairs (DCA). The statutory and regulatory powers to SEBI have been given by the Government with the mission to move from control regime to prudential regulations.

SEBI introduced a new clause 49 in the listing agreement of the stock exchanges vide its circular (SM/DRP/Policy/CIR-10/2000) dated 21st February, 2000, specifying the principles of corporate governance. Thereafter it issued circulars on 9th March, 2000, 12th September, 2000, 22nd January, 2001, 16th March, 2001, and 31st December, 2001, inter alia detailing provisions of corporate governance, its applicability, reporting requirements, amendments to clause 49. Following the recommendations of Narayana Murthy committee on corporate governance SEBI, in exercise of powers conferred by Section 11(1) of the SEBI Act 1992, read with Section 10 of the SCRA Act, 1956, revised clause 49 again vide its circular (SEBI/MRD/SE/2003/26/08) dated 26th August, 2003. But this circular was deferred for implementation and finally withdrawn by SEBI due to its controversial and debatable provisions. It was replaced by new SEBI circular (SEBI/CFD/DIL/CG/1/2004/12/10) dated 29th October, 2004, after complete overhaul of clause 49 (revised clause 49), superseding all previous circulars issued by SEBI in this regard.
The provisions of the revised Clause 49 must be implemented for the following entities:

- For entities seeking listing for the first time, at the time of seeking in-principle approval for such listing.
- For existing listed entities which were required to comply with Clause 49 which is being revised, i.e. those having a paid up share capital of Rs. 30 million and above or net worth of Rs. 250 million or more at any time in the history of the company, by April 1, 2005.
- The companies complying with the provisions of the existing Clause 49 at present must continue to do so till the revised Clause 49 is complied with or till March, 31, 2005, whichever is earlier.
- For other listed entities which are not companies, but body corporates (e.g. private and public sector banks, financial institutions, insurance companies etc.) incorporated under other statues, the revised Clause 49 would apply to the extent that it does not violate their respective statues and guidelines or directives issued by the relevant regulatory authorities. The revised Clause 49 is not applicable to mutual funds.

The main requirements of the revised Clause 49 of the Listing Agreement are summarized hereunder:

- Mandatory requirements (Annexure 1 of Clause 49) includes composition of Board, Non-executive Directors’ Compensation and Disclosures, code of conduct, composition of Audit committee, meetings, role, powers of Audit committee, related party transaction, CEO/CFO certification or Compliance etc.
- Non-mandatory requirements (Annexure 1 D of Clause 49) includes Maintenance of Board, composition of remuneration committee, shareholders rights, Auditor qualification, Training of Board members, Mechanism for evaluating non-executive Board Members or Whistle Blower Policy etc.

Recently, SEBI has added some new provisions in the Clause 49 of the Listing Agreement which stipulate that:
- If the non-executive chairman of a listed company is a promoter or is related to the promoters or persons occupying management positions at the board level or one level below the board, at least one-half of the board of the company should consist of independent directors.
- An independent director should have a minimum age of 21 years.
- The time gap between the exit and entry of independent directors shall not exceed 180 days.
- The disclosures of relationships between directors shall be made in documents and filing.

### 2.6 Comparative Study between Clause 49 of the Listing Agreement & Sarbanes Oxley Act, 2002

The Sarbanes Oxley Act, which was signed by the US President George W. Bush into law in July 2002, has brought about sweeping changes in financial reporting. This is perceived to be the most significant change to federal securities law since 1930s. Besides directors and auditors, the act has also led down new accountability standards for security analyst and legal counsels.

In India, the CII took the lead in framing a desirable code of corporate governance in April 1998. This was followed by the recommendations of the Kumar Mangalam Birla Committee on corporate governance. This committee was appointed by SEBI. The recommendations were accepted by SEBI in December 1999 and now enshrined in Clause 49 of the listing agreement of every Indian Stock Exchange.
Some of the major differences between Clause 49 & Sarbanes Oxley Act, 2002 are as follows:

2.6.1 Internal control:

Clause 49(revised)

CEO/CFO accept responsibility for establishing and maintaining internal controls and that they have evaluated the effectiveness of the internal control systems of the company and they have disclosed to the auditors and the Audit committee, deficiencies in the design or operation of internal controls, if any, of which they are aware and the steps they have taken or propose to take to rectify these deficiencies. The role of audit committee is to review this internal control report.

Sec. 302 of Sarbanes-Oxley

The principle executive officer or officers and the principle financial officer or officers or persons performing similar functions have the responsibility of designing, establishing and maintaining the internal controls. Here in the Sarbanes Oxley Act the public company accounting oversight board will review the same and not the audit committee.

In Clause 49 the audit committee will review the internal control mechanism whereas as per the Sarbanes Oxley Act the public company accounting oversight board will review the same. In Clause 49 Internal Control is only specified but no elaborative details are given about it whereas in Sec. 404 of the Sarbanes Oxley act the details regarding the same are specified.

2.6.2 Audit Committee composition:

Clause 49 (revised)

1. The audit committee shall have minimum three directors as members.
2. Two-thirds of the members of audit committee shall be independent directors.
3. All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise.
In Sarbanes Oxley act the number of directors constituting the audit committee is not specified. Also the frequency, the time gap between the meetings of audit committee is not specified. These points are clear in the Clause 49.

Section 301 of Sarbanes-Oxley
The committee (or equivalent body) is established by the board of directors of the issuer for the purpose of overseeing the accounting and financial reporting processes of the issuer. If there is no such committee then the entire board of directors is considered to be the member of the audit committee. Each member of the company's audit committee must be a director and must otherwise be independent.

2.6.3 Independent Director:
As per Clause 49 (revised)
For the purpose of the sub-clause (ii), the expression ‘independent director’ shall mean a non-executive director of the company who 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. He is not related to promoters or persons occupying management positions at the board level or at one level below the board. He has not been an executive of the company in the immediately preceding three financial years. He is not a partner or an executive or was not partner or an executive during the preceding three years, of any of the following:
- The statutory audit firm or the internal audit firm that is associated with the company.
- The legal firm(s) and consulting firm(s) that have a material association with the company.
He is not a material supplier, service provider or customer or a lessor or lessee of the company, which may affect independence of the director. He is not a substantial shareholder of the company i.e. owning two percent or more of the block of voting shares.
As per the clause 49 the definition of the independent director is wider in scope than the one in Sarbanes Oxley Act.

As per Sarbanes-Oxley
In order to be considered independent the one who does not

1. Accept any consulting, advisory or other compensatory fee from the issuer.
2. Be an affiliated person of the issuer or any subsidiary thereof.

2.6.4 Shareholders / Investors complaints:
Clause 49 (revised)
Shareholders section in the disclosures of clause 49 states that a board committee under the chairmanship of a non-executive director shall 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’.

Sarbanes Oxley act mainly considers the accounts related queries whereas Clause 49 covers the topic in the broad sense.

Sec. 301 of Sarbanes-Oxley
As per this section, each audit committee shall establish procedures for

1. the receipt, retention and treatment of complaints received by the issuer regarding accounting, internal accounting controls or auditing matters and
2. the confidential, anonymous submission by employee of the issuer of concerns regarding questionable accounting or auditing matters.

2.6.5 Penal Provisions:
Clause 49 (revised)
For violation of the listing agreement, Section 23E of Securities Contract Regulation Act, 1956 provides for a pecuniary penalty of up to Rs.25 crores on the company.
Sec. 302 of Sarbanes-Oxley
For violation of Sarbanes-Oxley Act, Section 906 imposes fines and imprisonment of up to $1 million and 10 years for knowing violations of Section 906, and up to $5 million and 20 years for willful violations.

2.6.6 Code of Conduct/Ethics:
Clause 49(Revised)
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. For this purpose, the term "senior management" shall mean personnel of the company who are members of its core management team excluding Board of Directors. Normally, this would comprise all members of management one level below the executive directors, including all functional heads.

As per the above paragraph, in the Indian context, it will be obligatory for the board of the company to lay down a code of conduct for the board members and the senior management of the company.

Section 406 of Sarbanes-Oxley
The act directs the companies to disclose if they have adopted code of conduct, if not, reasons thereof. Issuers shall adopt a code of ethics for senior financial officers, applicable to its principal financial officer and comptroller or principal accounting officer, or persons performing similar functions.

As per Sarbanes-Oxley, it restricts the code of conduct to be applicable to only 'principal financial officer and comptroller or principal accounting officer, or persons performing similar functions
2.6.7 Public Company Accounting Oversight Board (PCAOB)

As per the Sarbanes Oxley act, a Public Company Accounting Oversight Board has been set up to oversee the audit of listed companies in order to protect investors’ and public interest in matters relating to the preparation of audited financial statements.

There is no such provision in the Clause 49. In India the ICAI is legally empowered to carry out most of the regulatory, oversight and disciplinary functions outlined in the SOX Act (barring prosecution and levying of penalties). But the public perception is that the ICAI mechanisms are slow and the institute is not interested in adequately disciplining the members. In India the functions of PCAOB are carried out by various regulatory agencies viz. SEBI, RBI, ICAI, ICSI, ICWAI etc. If there were to be an Indian version of the PCAOB, then such powers would need to be withdrawn from the existing regulatory agencies and concentrated in the proposed public oversight board.

2.7 Amendments to the Companies Act, 1956

India took up its economic reforms programme in 1990s. Again a need was felt for a comprehensive review of the Companies Act, 1956 which has become the bulkiest and archaic with 781 sections and 25 schedules by this time. Three unsuccessful attempts were made in 1993, 1997 and then in 2003 to rewrite the company law. Companies (Amendment) Bill, 2003 which contained several important provisions relating to corporate governance was withdrawn by the Government in anticipation of another comprehensive review of the law. As many as 24 amendments to this Act were made since 1956, of which the

The important amendments having overall implications for corporate governance are listed below:

2.7.1 The Companies (Amendment) Act, 1999
- Buy back of shares (Section 77A)
- Issue of sweat equity shares (Section 79A)
- Establishment of investor education and protection fund (Section 205(c))
- Liberalization of Inter-corporate loans and investment norms.

2.7.2 The Companies (Amendment) Act, 2000
- Penalties increased by almost ten times for non-compliance in various Sections of the Act
- Issue of shares with differential rights (Section 86)
- Passing of resolutions by postal ballot (Section 192A)
- Directors’ Responsibility Statement (Section 217(2AA))
- Additional powers and duties of auditors (Section 227)
- Minimum number of directors including election of small shareholders’ director (Section 252)
- Maximum number of directorships in companies reduced from 20 to 15 (Section 275)
- Audit Committee (Section 292A)

2.7.3 The Companies (amendment) Act, 2009
Some of the amendments to the companies Act which are remarkable and have a direct bearing on improvement in the standards of corporate governance are explained below:
- Passing of resolution by Postal Ballot (section 192A)
Instead of transacting the business in the general meeting, public listed company, resolutions relating to such business as the central government may, by notification, declare to be conducted only by Postal Ballot.

The company when decides to pass resolution by postal ballot, it shall send a notice to all shareholders by registered post.

If a resolution requires requisites majority of the shareholders by means of postal ballot, it shall be deemed to have been duly passed at a general meeting convened in that behalf.

Under Directors’ Responsibility Statement (217(2AA)) section, the board’s report shall include a ’Directors’ Responsibility Statement’. 