Need of Effective Corporate Governance and Its Challenges in India

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Abstract
Corporate governance is the set of processes, policies, to ensure proper management of companies for effective accountability to all stakeholders, aim to optimize economic output and protect the interest of shareholders. It includes in its orbit all implicit and explicit relationships between the corporation and its employees, customers, creditors, suppliers and all other stakeholders. Government of India has taken policy step to provide direction, control and guidelines to all companies to work in ethical ways, create trust among shareholders and customers, to provide stability to our economy and to check financial scams and frauds. Regulations formed by different committees, need of effective corporate governance and challenges to corporate governance are briefed in this paper.

Keywords: corporate governance, principles of corporate governance, regulations in India, effectiveness, current position, tolerance level.

Introduction
Corporate governance is about ensuring that a business performs well through the adoption of fair and ethical principles and those investors receive a reasonable return. The governance framework provides the overall direction to management and ensures accountability to shareholders and other stakeholders. Corporate governance exists at a complex intersection of law, morality and economic efficiency. Corporate governance is expected to follow the principles of fairness, transparency, accountability, responsibility, maximising business performance and global competition. Corporate governance deals with effective strengthening of the investors and creditors rights.

According to the noble laureate Milton Friedman, “Corporate governance is to conduct the business in accordance with owner or shareholders desire, which generally will be to make as much money as possible, while conforming to the basic rules of the society embodied in law and local customs.”

Corporate governance is concerned with holding the balance between economic and social goals and between individuals and company goals. The corporate governance frame work is there to encourage the efficient use of resources and accountability for the stewardship of these resources. Its aim is to align as nearly as possible to the interest of individuals, corporations and society.

REGULATIONS FOR CORPORATE GOVERNANCE IN INDIA
Many financial scams have forced to set up corporate governance in India. Concentrated ownership of shares, pyramiding and tunnelling of funds among group companies has marked the Indian corporate landscape. Unethical and illegal operations during 1990-2000 have forced the business sectors to adopt corporate governance. Corporate governance and economic development are intrinsically linked. Effective corporate governance system promote the development of strong financial system irrespective of whether they are largely bank-based or market based which in turn have an unmistakably positive effect on economic growth and poverty reduction.

Good corporate governance is characterised by firm commitment and adoption of ethical practices by an organisations across its entire value chain and in all its dealings with a wide group of stakeholders encompassing employees, customers, vendors, regulators and shareholders.

The ministry of corporate affairs has proposed the New Companies Bill 2008 which aims to improve corporate governance by vesting powers in shareholders. These powers have been balanced by greater emphasis on self-regulations, minimization of regulatory approvals and increased and more transparent disclosures of financial matters.

The most important development in the field of corporate governance and investor protection in India has been the establishment of the Securities and Exchange Board of India in 1992. In 1996 a committee chaired by Rahul Bajaj had developed confederation of Indian industry code for desirable corporate governance. In 2000, Kumar Mangalam Birla committee and in 2003, Narayana Murthy committee had given their reports regarding corporate governance. These committees have the maximum impact on changing the corporate governance situation in India. These three committees have given norms related to creditor’s rights, shareholder’s right, special disclosure for initial public offering, transparency in financial dealings appointing board of directors.

The advisory group of RBI, Standing committee on International financial standard and codes had submitted its reports in 2001. Recommendations of Birla committee were implemented through the enactment of clause 49 of the listing agreements. These recommendations were applied to

2. Companies with a paid up capital of Rs 10 crore or with a net worth of Rs 25 crore at any time in the past 5 years.
3. Other listed companies with a paid up capital of over Rs 3 crore on march, 2003.
4. Much attention to the subject of share transfers.

From 1994, the board of financial supervision has been inspecting and monitoring banks using CAMELS (Capital adequacy, asset quality management, earnings, liquidity and
system controls) approach. Audit committees in banks have been stipulated since 1995\(^5\).

The important legislation for regulating the entire corporate structure and for dealing with various aspects of governance in corporations are companies Act, 1956 and companies Act Bill, 2004. The securities contract (regulations) Act, 1956, securities and exchange board of India Act, 1992 and depositories Act, 1996 have been introduced by securities and exchange board of India with a view to protect the interest of the investors in the securities market so as to maintain the standards of corporate governance in the country. Securities contract (Regulation) amendment Act, 2002 has been enacted in order to amend the securities contract (Regulations) Act, 1956, with a view to include securitisation instruments under the definition of securities and provide for disclosure based regulations for issue of the securitised instruments. The security and exchange board of India has specified the matters relating to misuse of capital, transfer of securities and other matters such as manner in which such matters shall be disclosed by the companies. Depositories Act, 1996, provides for the introduction of scrip less trading system and settlements, which is considered necessary for the effective functioning. The companies Bill, 2004 contains important provisions relating to corporate governance like independent auditors with management of company, independent directors with a view to improve the corporate governance practices in the corporate sector. It is subjected to greater flexibility and self-regulations by companies. Better financial and non-financial disclosure and more efficient enforcement of law.

**EFFECTIVE CORPORATE GOVERNANCE**

There are few features of effective corporate governance:

1. Access to external financing which will lead to greater investment, growth and employment
2. Lower the cost of capital to reduce risk of financial crisis.
3. Better resource allocation to win trust of stack holders, to improve social and labour relations and for environment protection.
4. Transparency in all financial and non-financial matters.

**CURRENT POSITION OF INDIA IN WORLD SENARIO**

According to the CLSA Corporate Governance Watch 2012 list, produced in collaboration with the Asian Corporate Governance Association, India's corporate governance score has improved by 3 percentage points but ranking has remained the same.

“This is not due to a lack of awareness by the regulators, but rather a piecemeal approach to reform and a lame duck government unable to do anything meaningful given infighting among its allies,” ACGA Research Director Sharmila Gopinath said in the report. Among the market rankings, Singapore was at the top in 2012 followed by Hong Kong and Thailand in the second and third position respectively. In the fourth position there is a tie between Japan and Malaysia, the report said. Others in the top include Taiwan at the 6th place, followed by India (7th), Korea (8th), China (9th), Philippines (10th) and Indonesia (11th). The report which analysed as many as 864 listed companies across Asia-Pacific markets, including Japanese and Australian firms, said that Infosys was the only Indian company that was featured in the top 20 corporate governance large caps. Moreover, there were just five Indian companies which got featured in the top 50 league table. Besides, Infosys the other four include HUL, Wipro, Titan Industries and Yes Bank.

"Despite efforts made by the corporate sector and individual regulators to raise corporate governance standards, these mostly fail to address core governance issues such as accounting standards, the regulation of auditors and obstacles to voting for investors who are unable to attend company meetings," Gopinath added. The report, entitled "Tremors and cracks", noted that cracks in Asian corporate governance have become more apparent with corporate scores slipping since the previous CG Watch report was issued in 2010. Investors have faced issues ranging from relatively minor corporate transgressions to growing concerns about the reliability of financial statements and, at the extreme, outright fraud. "Corporate governance is largely about checks and balance,“ CLSA Head of Asia Research Amar Gill said in a statement, adding that "Investors will need to swerve and get a tighter grip when dealing with the cracks in governance and the tremors in Asian investing."\(^5\)

**CHALLENGES TO EFFECTIVE CORPORATE GOVERNANCE**

There are some practices prevalent in the market and in our society which are posing challenges to corporate governance in our country.

1. Unsophisticated equity market vulnerable to manipulation and with rudimentary, traditional analyst activity.
2. Dominations and monopoly of family firms.
3. High level of corruption, become visible only after a revelation of big financial scam.
4. Weak and non-transparent monitoring system.
5. Lack of respect for shareholders and low financial disclosure.

The perception of poor corporate governance in public sector enterprises can be a dampener for the government’s divestment programme. The government is hoping to raise Rs 30,000 crore by share sales in companies such as Steel Authority of India Ltd, Bharat Heavy Electricals Ltd, NMDC Ltd, National Aluminium Co Ltd, Oil India Ltd, Rashtriya Ispat Nigam Ltd and MMTC Ltd. In a new low, the recently released government data showed many state-owned firms are not even keen to self-evaluate their governance standards. As per data released by the Department of Public Enterprises (DPE) on Monday, out of the 249 central public sector undertakings in the country, 109 entities did not provide self-evaluation reports on their corporate governance practices for 2010-11.

According to a recent survey by the Confederation of Indian Industry and Institutional Investors Advisory Services, investors rated the governance in state-owned companies at 1.75 on a scale of four, much below 3.67 for multinational corporations and 3.17 for professionally-run companies. This low perception of governance in turn resulted in poor return expectations. Public sector undertakings (PSUs) came last among the four categories of companies in terms of perceived shareholder returns. At the score of 1.36, PSUs were behind even promoter-run companies, which had a lower governance score.
While the share prices have improved considerably riding on a series of government decisions and cheap and easy money around the globe, the government’s lack of concern for governance issues, including protection of minority investor rights, are seen as key risks by institutional investors. The government is often accused of treating listed PSUs as its hand maidsens using their balance sheets to fund populist schemes. In 2009, Goldman Sachs had slammed the government for using Oil and Natural Gas Corp’s balance sheet to subsidise fuel prices. At present, the UK based hedge fund TCI is in the middle of a messy public spat with the government for allegedly following pricing policies that are detrimental to shareholder interests. The CII-IIAS survey showed investors have very low tolerance levels for corporate governance issues in the investee companies. “About 33 per cent of the investors expect corporate governance issues to be resolved within one month, while 42 per cent expect corporate governance issues to be resolved within three months. In other words, institutional investors have a very low tolerance for bad corporate governance, and may respond by exiting the company,” it said. Although PSUs received a very low rating in terms of perceived shareholder returns (rated 1.36), they have fared better when investors have been asked to rate their likelihood of investing in them (rated 2.33). “In the current environment it implies investors expect some favourable policy changes,” the IIAS report said.6

SUGGESTIONS FOR EFFECTIVE CORPORATE GOVERNANCE
Due to social, economic and political obstacles in the way of effective corporate governance, there is need to adopt some measures.

1. Efficient monitoring system can improve transparency in business management.
2. Adoption of a transparent process of appointment at board and management levels.
3. Proper checks and balance system over managerial rights.
4. Accurate informations regarding developments, threats and risks related to financial and economic matters in annual reports and on the company websites.
5. Proper and transparent auditing system to check financial irregularities and frauds.
6. Codes of conduct are ensured to be understood and adhered to by all members of organisation.
7. Ethical behaviour of organisation or of any member at board or management level should be rewarded.
8. There should be an independent and transparent process of evaluation of performance of board members.

CONCLUSION
Corporate governance has been proving a very efficient and effective system for our economy and to save the interest of shareholders but some more efficient monitoring and transparent internal audit system, efficient board and management can lead it to effective corporate governance.

REFERENCES: