ANALYSING THE EVOLUTION OF CORPORATE GOVERNANCE LAWS AND EXAMINING THE ROLES OF CORPORATE GOVERNANCE LAWYERS IN INDIA

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ABSTRACT

This paper deals with the development of corporate governance laws in India. Corporate governance is a term that is widely used to refer to the systems, policies and processes that enable companies to conduct their business in an ethical manner, corporate governance since attaining its prominence in the 1980s has revolutionized the corporate world. The need for better corporate governance has increased phenomenally since the unravelling of India's biggest corporate fraud and governance scandals in the Satyam case, therefore this paper aims at analysing the evolution of corporate governance at different stages of the growth of India's corporate sector. The paper also discusses formulating a legal framework for proper corporate governance and analyses the trend of corporate governance incorporated in India's most successful business ventures. The paper also elucidates the importance of corporate governance lawyers and their roles in developing and safeguarding corporate governance for the furtherance of corporate entities. The paper gives a structured study on corporate governance laws in India and the development of such laws by illustrating case laws and examples, thereby taking a real-time approach to exploring various problems and solutions concerning the same. The research objective is to investigate multiple existing corporate governance laws and, through extensive research and criticism, try to recognise the most effective practices to be incorporated by a corporate entity to succeed in the modern era while also examining the need for corporate governance lawyers and the specific roles and responsibilities of such profession.

INTRODUCTION

Corporate governance is all such policies, procedures or actions which affect the way a corporation is administered or directed. It also describes the relationship between stakeholders of the company and also furthers the interests of the company. The concept of corporate governance in the present world has attained much significance because it is responsible for the systemic and well-organised governance of daily corporate affairs and also accountable for complying with the legal necessities and regulatory provisions. Corporate governance is at the epi-center of corporate management which has the power to deliberate upon legal compliances, achieving business goals and reaching the targeted financial goals.

In response to this many companies are articulating their own corporate governance policies and procedures to set-forth certain protocols to be followed in terms of: 1) Administration and management of company affairs, 2) Effective dispersal of company's operations, 3) Monitoring the conduct of company personnel (e.g., offences under POSH Act[1]), 4) Handling client interactions and 5) Adhering to the rules and regulations laid out by the regulatory authorities. While formulating the corporate governance policies form one side of the coin the execution of such policies and procedures with precision forms another side of the coin.

The primary objective of any company would be to increase their stakeholder value and thereby require the faith of the society to do that hence they must adhere to the values and norms of the society they are a part of. Good corporate governance forms a huge part of achieving this goal of companies. In the tail end of the 20th century, the public's trust in the corporation's ability of self governance was low, as a number of scandals were brought to light and the investor's confidence got rattled the governments of different nations sought to develop their own regulatory framework to deal with such scandals and frauds. In the United States for example the Public Company Accounting Reform and Investor Protection Act was introduced which laid down legal obligations on both publicy traded companies and privately held corporations and Cannada followed suit with Bill C-198.

In India the organizational structure for corporate governance initiatives included the Ministry of Corporate Affairs(MCA) and the Securities and Exchange Board of India(SEBI). SEBI is responsible for the monitoring and regulation of of corporate governance in the publicly held

[1] PoSH (Protection of Women from Sexual Harassment) Act, 2013

companies through Clause 49[2] . MCA is also responsible for appointment of committees and forums such as the National Foundation for Corporate Governance (NFCG) which is forum for exchange of ideas and experiences amongst corporate leaders, regulators and law enforcing agencies and non- government organizations.

The Companies Act, 2013, the new legislation repealing the old Companies Act 1956, also provides a formal structure for corporate governance which through new compliance norms enhances disclosures, reporting and transparency in the corporate entities. Apart from this, the Competition Act, 2002[3], the Foreign Exchange Management Act, 1999[4], the Industries (Development Regulation) Act,1951 and other legislations also contain provisions relating to corporate governance. There are also numerous acts and guidelines formulated by various other regulatory and non-regulatory bodies[5] on corporate governance throughout the history of the existence of corporate governance. The Kumar Mangalam Birla Committee (2000) set up by SEBI takes credit for recommending the addition of Clause 49 in the Listing Agreement to promote good corporate governance. "On 21 August 2002, the Ministry of Finance appointed the Naresh Chandra Committee to examine various corporate governance issues primarily around auditor – company relationship, rotation of auditors and defining Independent directors. This was followed by constitution of the Narayana Murthy Committee (2003) by SEBI, which provided recommendations on issues such as audit committee's responsibilities, audit reports, independent directors, related parties, risk management, independent directors, director compensation, codes of conduct and financial disclosures. Many of these recommendations were then incorporated in the Revised Clause 49 that is seen as an important statutory requirement."[6] Since the new Companies Act, 2013 was enacted SEBI has amended Clause 49 in accordance with the Act.

Lawyers play an important role in corporate governance in the present era because as stated above there are various statutory regulations imposed on corporate governance and these regulations have to be adhered to by the companies and hence such a task can be successfully done only with the backing of a person well versed in the field of corporate laws and hence the

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[2] This clause is incorporated in the listing agreement of stock exchanges with companies and it is compulsory for listed companies to comply with its provisions

[3] Replaced the Monopolies and Restrictive Trade Practices Act, 1969

[4] Replaced the Foreign Exchange Regulation Act,1973

[5] For example, Desirable Corporate Governance Code by the Confederation of Indian Industries (CII) in 2009

[6] https://www2.deloitte.com/in/en/pages/risk/articles/governance-101.html

profession of corporate governance lawyers came into existence. They are basically business consultants and advice corporate leaders in various decision making processes.

II. CORPORATE GOVERNANCE LAWS: A STUDY

A. HISTORY

The concept of corporate governance has attained prominent status only since the 1980s and mainly after the issuance of code of corporate administration issued by the Cadbury advisory group[7]. The committee in its report related to Financial Aspects of Corporate Governance distributed in 1992 recognised the term "corporate governance" as "the framework by which organisations are coordinated and controlled". In India, with consideration to the Cadbury Council, the Kumar Mangalam Birla Committee issued a code of corporate administration for corporate entities in India. As per the corporate culture prevalent, directors are responsible for the administration of the company and the role of the investors in administration is to choose the directors and administrators and fulfill themselves that a fitting administration structure is set up[8].

Prior independence Indian associations were by colonial guidelines and they were predominantly in favour of the interests of British employers. The Companies Act was enacted in 1866 and amended in 1882, 1913 and 1932 and the Partnership Act was enacted in 1932, this was the period of test and trial method where laws were liberal and led to misuse and abuse of resources and high managerial persons evaded their responsibilities towards frauds and such unethical practices.

After the independence there was boom in the industries producing essential items of which the government dictated the prices. The Industries (Development and Regulation) Act and Companies Act were introduced in the 1950s and in 1960s the setting up of heavy industries occurred and 1970s to 1980s involved the evolution of cost accounting activities. There were some endeavours made by certain companies to create a standard framework for good corporate governance and is also at par with the international standards but due to lack of encouragement theses norms became too promoter centric and hence became impractical. The first

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[7] The London Stock Exchange and the Bank of England set up a committee in 1991 under the Chairmanship of Sir Adrian Cadbury to look into the financial aspects of corporate governance

[8] Anubhav Pandey, Regulatory Framework for Corporate Governance in India, iPleaders, 20-5-2017 <https://blog.ipleaders.in/corporate-governance/>.

fundamental code for corporate governance was suggested by the Chamber of Indian Industries (CII) in 1988. The definition provided by CII was - " corporate governance manages laws, methods, practices and understood principles that decide an organisation's capacity to take administrative choices—specifically its investors, banks, clients, the State and the representatives."

B. IMPORTANCE/ REFORMS

The primary aim of the India's corporate governance reforms were to make Audit Committees[9] and Boards more independent, providing powers to the supervisors of the company management and creating procedures to help shareholders including the foreign investors. These reforms were mainly introduced through the Ministry of Corporate Affairs (MCA)[10] and SEBI as regulatory bodies. The CII in 1966 was the first to take a crucial step in corporate governance, its aim was to create a framework for corporate entities be it private or public. This step was mainly with respect to protecting the interests of the investors and also to create a transparent atmosphere within the business to protect the interests of small investors and also to increase confidence in people with regard to investing.

The report of the Kumar Mangalam Birla Committee on corporate governance was also one of significance because the companies by signing the listing agreement had to disclose separately in their annual report the initiatives they have taken to amend their corporate governance as per the recommendations of the committee. This was to ensure the stakeholders that the companies they have invested in have a foolproof corporate governance or not. The committee also suggested important recommendations relating to the constitution and the functioning of the Audit Committees. The SEBI amended its listing agreement to include the new rules and regulations under Clause 49 which came into force in phases from 2000 to 2003.

The advisory group[11] on corporate governance in its report compared the standard of Indian corporate governance practives and framework to the the international standards and suggested that India had to improve corporate governance standard. In 2001, there was a report by the

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[9] Audit committee refers to one of the key committees in a corporate form of organisation to oversee the discharge of statutory audit compliances by the company.

[10] The Ministry of Corporate Affairs is an Indian government ministry primarily concerned with administration of the Companies Act 2013, the Companies Act 1947, the Limited Liability Partnership Act, 2008, and the Insolvency and Bankruptcy Code, 2016.

[11] Standing Committee on International Financial Standards and Code—March 2001

Consultative Group of Directors of Banks in which the corporate governance of directors of banks and other financial institutions was constituted by the Reserve Bank with the aim of getting constructive feedback from the boards of directors with respect to compliance, transparency and accountability; thereby providing suggestions as to how the role of Directors in a company can be made more effective.

The Naresh Chandra Committee in 2002 provided a report on corporate governance and audit which recommended improvements in ares like statutory auditors, independence of auditors, procedure for their appointments, their fee structure and other such issues with an aim to produce a true and fair financial statement of the company. SEBI in 2003, produced a report under the Murthy[12] Committee which had the objective of improving governance policies through the study of role of independednt directors, related party transactions, terms related to directorship and their remuneration, risk management policies and code of conduct and financial transperancy.

Clause 49 Amendment was the by-product of the Murthy Commtittee, however the implementation of the same had been postponedto 2006 because of lack of preparation and the sudden changes proposed which left industries in awe. Nevertheless there were certain changes brought about with relation to corporate boards, audit committees and CEO/CFO certification of internal controls formed the largest of changes proposed to the governance.[13]

C. SATYAM CASE: A BREAKTHROUGH

The 2008 economic crisis hit the whole world pretty hard and India was not an exception, during this time India wasn't only going through a financial crisis but also an ethical crisis where the basic financial information provided by companies listed in the stock market were being manipulated. The Satyam case is a classic example of this scenario. Satyam during it peak had a flawless reputation for conducting business and they were acknowledged for the same through various acumen as well. But everything started to get blurry when Mr. Raju who was the managing director of Satyam decides to buy his own real estate company through the company for which there was a huge outcry against such purchase by its shareholder and during this time the stock prices of Satyam plummeted and soon enough everything fell apart. On

[12] Headed by N R Narayan Murthy
[13] (2019) PL (CL) November 69

January 7th, 2009 Mr. Raju resigned to his post and confessed to the manipulation of accounts of upto Rs. 7000 crores.

The scam was being concocted from fairly a long time behind closed doors, Mr. Raju inflated the numbers of quarterly profits in order to show that the growth was with par to the analyst's expectations, one example to the same would be the results announced on October 17, 2009 where the quarterly revenues were overstated by 75% and the profits by 97%. The whole was done with the help of the company's global head for internal audit. Mr. Raju through his personal computer manipulated the bank statements inflating it with cash records that didn't exist while company's global head for internal audit created fake customer details and fake invoices in order to inflate the revenue, while all of this allowed them to receive loans and also create an impression of a successful company thereby shooting up stock prices.[14]

The Satyam scandal can be considered as a catalyst for the Indian Government to reevaluate its mechanisms in place to check on corporate governance, disclosure, accountability and transparency. The CII immediately after the news of the scandal broke out began investigating the lacunae in the corporate governancepolicies encorporated by Satyam. The other industry groups also formed committees to study the corporate governance failure and the impacts of such failure. The CII after its investigation into the matter recommended certain reforms in 2009. According to its reports it was able to prove that the Satyam scam was just a one-off scam and that was not the case in the vast majority of the companies who had a fairly good corporate governance policies and also conducted their business ethically.

The Satyam case was not however the only landmark case with respect to the failure of corporat governance, there was the Ricoh case, ICICI Bank Scam Case, Kingfisher Airlines and United Spirits Case. All of these cases eventually led to a lot of reforms though these were some of the biggest scams in India they eventually led to the formation of more stringent policies leading to foolproof systems which eventually covered the lacunae in the Government's regulatory mechanisms.

D. CURRENT TRENDS

Firstly lets address the existing legal framework with regard to corporate governance, the

[14] Aron Almeida, Satyam Scam – The Story of India's Biggest Corporate Fraud!, Market, News, January 3rd 2022, https://tradebrains.in/satyam-scam/

Companies Act consists of provisions relating to the constitution of the board[15], board processes, board meetings[16], independent directors[17], audit committees[18], general meetings[19], related party transactions[20], disclosure of financial statements etc. The Companies Act, 2013 is a very important and prominent legislation which deals with the corporate governance in companies. The Companies Act has constantly evolved to fill in the gaps in the laws due to which any fraud or other unethical practices could be conducted.

SEBI also has issued guidelines, rules and regulations being the governing authority which has the jurisdiction and power over the companies listed on the stock exchanges. There are also conditions mentioned on the listing agreement of the stock exchanges. There are certain accounting standard set for a company by the Institute of chartered Accountants of India (ICAI) and there are certain secretariat standards set by the Institute of Company Secretaries of India (ICSI). These standards set by the institutions are important because these professions play an important role in corporate governance and hence there must be certain amount of transparency and integrity to be hel by persons of such profession.

In India, Hindustan Unilever Ltd., Housing Development Finance Corporation Ltd. and Infosys Ltd. are the top three best governed companies, also the overall corporate governance standards of the BSE 100[21] companies which form 72% of the total market capital is said to have increased according to the 'Stability Despite Headwinds' report which was published by a proxy advisory firm- Institutional Investor Advisory Services India Ltd., BSE[22] and International Finance Corporation. The parameters on which this assessment was based included board effectiveness, conflict of interest, stakeholder engagement, audit quality and executive remuneration.[23] The report also established a connection stating that well- governed companies reported a better price performance compared to the the companies which were not-so-well governed companies.

[15] Section 149, Companies Act, 2013
[16] Section 173(1), Companies Act, 2013
[17] Section 149(6), Companies Act, 2013
[18] Section 177, Companies Act, 2013
[19] Section 96, Companies Act, 2013
[20] Section 188, Companies Act, 2013
[21] The index is designed to measure the performance of the 100 largest and most liquid Indian companies within the S&P BSE LargeMidCap. The index is calculated in Indian Rupees.
[22] Bombay Stock Exchange
[23] Bloomberg Quint, https://www.bloombergquint.com/markets/best-companies-in-india-indias-best-governed-companies-list-has-three-new-entrants

To elaborate upon the parameters on which the governance policies of a company was assesed:

1) Board Effectiveness- In which two points mattered a lot i.e. the need to have a non-promoter director with certain domain experience on the board so that they challenge the assumptions made by the management while taking decisions and also the improvement in attendance of board meetings.

2) Conflict of interest- There was huge lack of such policy in many companies and even if it existed it was primarily limited to the upper or the senior management, hence a CoI policy for conflicts faced by the employees showed improvement in governance.

3) Stakeholder Enaggement- The acceptance of anonymous complaints without any fear of retaliation or hesitation was also a parameter on which the companies were judged. Also the existence of a foolproof whistleblower mechanism was a criterion so that the anonymous letters don't release to the public and undergo a media trial because such trial-by-media shall result in investor panic and eventually a decline in the stock price of the company.

4) Audit Quality- Audit quality forms an integral part of a company and should be up to a specific standard and this is essential to maintain the integrity of the company and the confidence of the investors. But unfortunately in India according to the above-discussed report less than half of the audit firms actually adhere to the generally accepted standards and the ICAI's Quality Review Board is responsible for reviewing the audit quality.

The companies that are currently performing well under these parameters are the classic example of how good corporate governance can lead to overall success. Ethical behaviour and good corporate governance often lead to creating a prominent public image in turn raising the company's market capital. Since we already know that only cooking profits and inflating the revenue without good corporate governance can only lead to negative effects for a company as seen in the Satyam case.

III. CORPORATE GOVERNANCE LAWYERS: THE NEED

A. IMPORTANCE

The main reasons why companies fall into trouble with respect to complying with the corporate governance standards and end up paying hefty fines is due to not having an effective legal department functioning in the organizational structure or inefficient personnel engaged in such

departments. There are always companies who tend to ignore the importance of an efficient legal system which is required to make sure that the company is adhering to proper legal compliance and regulatory requirements, these companies try to cut expenses but the fact of the matter is that cost-benefit analysis provides the benefit of the doubt to have an efficient legal department on board to not having one.

The realisation to have a proper legal team on board doesn't really occur to these companies until they are levied high fines or subject to legal proceedings in court. So these companies fail to recognise that the legal departments form the strategic and advisory part of an organisational structure thereby guiding the decisions of the management while adhering to the law.

There are numerous instances where companies failing to comply with statutory regulations and legal procedures end up facing heavy penalties and prosecution for violations come to be defunct companies, some even defrauding banks, shareholders and the economy at large. In the major investigation conducted by the Indian Government, it declared around 2.2 lakh companies as defunct companies which were not in compliance with the mandatory legal and regulatory requirements which was imposed by the law. This shows the magnitude of the problems faced by the companies due to lack of proper legal supervision. The companies in this case overlooked the consequences of non compliance leading to conclusion of their business operation aslo getting the independent directors of such companies barred from attaining directorship again due to no fault of theirs. These companies could have easily avoided the circumstance of attaining the status as defunct companies by entrusting competent legal and compliance proffessionals. Day by day these laws are getting more stringent and the government plans to take serious action against companies who fail comply with the necessary legal standards.

The legal departments primarily has two roles, formulation and implementation. Formulation includes the articulation of strict company policies concerning corporate governance and also strong protocols to make sure the company is in compliance with all the legal requirements and is in good faith with the governement and its shareholders. Formulation of such foolproof policies require a competent and qualified legal department, such legal department shall be responsible to consult all the stakeholders involved and combine all the representations received from them to the draft policy. The legal team shall also consider the interests of the stakeholders and also the business interests of the company while drafting policies while

keeping them in line with the laws of the nation.[24]

Implementation process of the the policies drafted is very important because without proper implementation of the policies they are inefficient and pointless. The legal and compliance team of the organization shall be responsible for the proper implementation in a well-organised manner to make certain thet the organization they are employed by is following all the existing statutary and legal requirements.

B. ROLES AND RESPONSIBILITIES

Corporate governance lawyers play the role of business consultants and guide the management in the decision making processes. They represent business leaders and corporate investors with the essential importance given to relationship and communication. These lawyers must be well versed in the corporate laws and must have basic legal and business knowledge."Corporate governance lawyers have a strong knowledge of typical corporate trustee practices, laws, regulation, and of how a company identifies, describes, and forms the roles of its leaders and management. A corporate governance lawyer also acts as risk management, and advises clients that are in high-risk situations."[25]

They perform an advisory role to the board of directors and senior management on the matters of the constitution and operations of the board, roles and responsibilities of an independent director, defining the rights and privileges of the company, assessing and reviewing the performance of the board and the board committee, threat management, assesing the distribution of salaries, intraoducing new and efficient corporate governance policies and constantly updating the rules, rights, privilages of the company.

Corporate governance lawyers also counsel corporate clients on matters such as management, investor relations, business procedures and risk associated with it. They also counsel on matters such as conflict of interest arising within the company, issues related to transactions, terms of a merger, in the selection process of senior executives, any governmental issues relating to state,national and global issues.

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[24] Bhumesh Verma, Soolegal, ROLE OF LEGAL DEPARTMENT IN CORPORATE GOVERNANCE, https://www.soolegal.com/roar/role-of-legal-department-in-corporate-governance

[25] Upcounsel, Corporate Governance Law: Everything You Need To Know, https://www.upcounsel.com/corporate-governance-law

IV. CONCLUSION

The paper delves on the topic of corporate governance, its history and its importance. Corporate governance was a topic that was overlooked for a long time until the its true value was realised by the corporate entities this paper provides various examples, statistics and facts to show that a company with good corporate governance can achieve greater heights. Corporate governance has had a steady evolution and the government also has taken various measures to make sure that there is a proper standard set to which the companies must adhere to, the paper also provides a case study on the Satyam case which was a very pivotal circumstance which led to some important amendments in the field of corporate governance. The paper also provides with the statistics and current trends which are practiced by high performing companies. The parameters on which the corporate governance of companies are evaluated are also elaborated thereby trying to understand the whole concept in a detailed manner to provide solution to attaining an efficient and effective corporate governance structure.

The paper also talks about the profession of a corporate governance lawyer and the importance of a legal department to handle such issues. The importance of a legal department in handling the issues relagting to corporate governance is specifically highlighted in this paper. The roles and responsibilities of a corporate governance lawyer are also discussed thereby providing a detailed overview of the whole concept and allows the reader to understand such profession without overtiring the reader.