PERSPECTIVES

Perspectives on Corporate Governance

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In the backdrop of the Satyam scandal, which rocked corporate India in the early 2009, a seminar was organised at IIM Indore to sensitise the participants about corporate governance and brainstorm on various related issues. As the scandal involved one of the respected industries, which boasted of sound, proactive corporate governance practices, a need was felt to understand what unique pressure this industry faces which leads to episodes like these. Objective was also to understand whether this episode was just and aberration for the industry or it is a more broad-based problem facing the information technology industry.

Of course, as has happened in other parts of the world, every such scandal leads to the regulators re-looking at the corporate governance codes and hence more stringent regulations. The idea behind the seminar was to explore what can be done, going beyond the regulations, to make corporate governance a way of life for corporate India. This seminar presents views on corporate governance from four different angles.

S. Sandilya, Chairman, Eicher Motors Ltd.
Corporate Governance: Some Views and Experiences

Any organisation, whether a business or a non-profit, needs some kind of governance to ensure that it is run in a way that meets the expectations of its stakeholders. Corporate governance is about creating value for all stakeholders of the organisation in a sustained manner by following most legal and ethical means.

The real task of ensuring good corporate governance in a company lies with the board of directors, while every person in the chain who helps to create value for stakeholders needs to be governed. A successful organisation requires an alignment between three Ps - Purpose, Process and People. Corporate governance leads to robust processes in the organisation, which helps its people realise its purpose.

It is also important to understand why companies follow good corporate governance practices. Different companies have different motives. A large number of companies do it just because it is a legal obligation. A second set of companies do it because of the pressures of globalisation - these are particularly the companies who have intentions of accessing foreign capital markets or have to work with foreign clients or have to do business abroad. For them, it helps develop a trust amongst the foreign stakeholders that they are dealing with a company sound in transparency and ethical standards. A third motive is to show an image of a good corporate citizen so that your stakeholders trust you more. However, the most crucial fourth reason is for the companies who believe that following good governance practices is good for them. Such companies go beyond the letter of the law and practice corporate governance in its true spirit. We need more of these fourth type of companies to lift the overall standards of corporate governance in the country.

More important than understanding why organisations should have good corporate governance practices is to understand how they should improve these practices. The following steps will help any organisation improve its corporate governance practices:

- Comply with prevailing legal framework on corporate governance - this should not be just a tick box approach on compliance with various provisions, but companies should go beyond the minimum prescribed regulatory requirements.
- Have robust systems in place to ensure good corporate governance. More importantly, have monitoring mechanisms to gauge the effectiveness of these systems. Most of the corporate frauds that we have observed in recent past have not been because of the absence of sound systems being in place, but because of they not being adhered to.
- Define a set of values for the organisation - practice them, show that people at the topmost position also adhere to those. Lead by example. Let stakeholders know that the top management abides by what it talks. The ancient wisdom of "Yatha Raja Tatha Praja" captures the essence of this.
- Practice openness and transparency - let all your stakeholders know what you do and why you do.
- Encourage, nurture and enforce organisational and personal integrity.
- Have an effective internal and external communication system in place - it is not only important to practice good corporate governance, but also equally important to let your stakeholders know.

Some experiences at Eicher

Eicher Motors has been one of the few corporations in India who have been following sound corporate governance practices much before these were mandated by law. Some of the best practices worth mentioning are:

- Being a pioneer in India in having investors' meets in the late 1980s. Eicher had these meetings at various locations to make it convenient for the investors to attend them.
- Being a pioneer in having a supervisory board. This board is over and above the statutory board, which the companies are required to have. This board would comprise eminent people in the line of business, independent of the management. The function of this board was to focus mainly on strategy, controls and people, while being relieved from statutory duties. This was scrapped in 2004 as these functions were brought under the purview of the statutory board itself in the new corporate governance regulation.

- Having a robust process of selection of board members, which helped Eicher get independent professionals on board, much before it was mandated by the corporate governance code.

- Having a policy of not offering gifts to shareholders at the annual general meetings, while it was a common practice some time back.

- Having the practice of exclusive meetings with various stakeholders, to understand the aspirations of various stakeholders and also communicate the company's policies on corporate governance and ethical practices.

- Having a policy of not employing relatives of employees. This is practiced at every level in the organisation.

Good corporate governance starts with having a good self-governance or following self-discipline because only a team of self-governed individuals will lead to a self-governed corporation. Finally, to sum it all, it can be said that corporations with good corporate governance LAST, whereas corporations with bad corporate governance are LOST.

Asank Desai, Founder and Ex-Chairman Mastek India Ltd.
Significance of Corporate Governance for the IT Industry

Information Technology (IT) industry in India has grown in leaps and bounds since its modest beginnings in the 1990s. The industry is now close to $50 billion in size, which is a growth of approximately 1,000 times in a period of 20 years. This also means a compound annual growth rate of 40 to 45%, which would be the highest growth recorded by any industry for such a long continuous period. The industry contributes close to 6% to our general development procedure. Moreover, 79% of the industry revenue comes from export. A majority of this export is to the Anglo-Saxon countries (US accounting for 60% and UK for 19%). This fact itself is a driver of corporate governance in the IT industry in India. Practising good corporate governance becomes important for the IT industry as the customers it is dealing with are sophisticated and situated thousands of miles away from India.

This also explains why IT industry has been the pioneer in introducing improved corporate governance structures in India. The customer sitting miles away and planning to give a large mission-critical job to an IT company in India would like to make sure that the company is well placed to execute this task. This does not only mean that the company should have technical capabilities but also that it should have robust corporate governance practices.

IT industry in India derives most of its export revenues from three sources - custom application development, application maintenance and BPO services. The BPO services are even more mission-critical for the customers of Indian IT industry because there we are managing client's business processes. Sustainability of clients or the value of client in the minds of their own customers depends on the strengths of these business processes. Because it is very critical for the client, he wants to ensure that these processes are run by companies that have high ethical standards, value sets and governance systems in place. A good example of this was the alleged credit card data theft scandal where India-based BPO employees, who were handling their customer relationships, leaked a client's customer information. Of course, the customer companies would like to avoid such instances.

Another thrust to corporate governance for IT companies comes from the kind of employee base these companies have. IT industry in India employs close to 2.2 million people directly, and with a multiplier effect of 3.6 times, it generates indirect employment of about 8 million jobs. We, thus, have about 10.2 million employees linked to this industry. More importantly, the workforce in the industry is entirely of highly qualified knowledge workers who are sensitive to the issues of corporate governance. Attracting and retaining good-quality workforce requires these companies to project an image of being highly professional and ethical companies.

Yet another pressure for following good corporate governance practices in the IT industry is the unique shareholding structure these companies have. Most of the IT companies in India have significant holdings (16-20% on an average) from foreign institutional investors and many of them also have their customers as their shareholders. There is always a pressure from these shareholder groups that the company adhere to the best practices of corporate governance.

One of the important issues as regards to corporate governance, which is important for IT industry, is the issue of risk management and mitigation. Risk management has been historically given high importance by the industry. Most of the companies have elaborate system of identifying potential risk areas and reporting back to the board of directors, the steps taken by the company to mitigate them.

Due to these pressures, IT industry in India has been one sector which has been ahead of others as far as corporate governance implementation is concerned. IT industry players have been rated high in corporate governance by most rating agencies. This effect has also trickled to other industries and improved the overall corporate governance climate in India.

Kamlesh S. Vikamsey, CA, Partner Khimji, Kunwarji and Company
Corporate Governance and the Role of Audit Function

Corporate governance is about maximising shareholders' value, legally, ethically and on sustainable basis, ensuring fairness to every stakeholder. The objective of corporate governance is to ensure three things - first is the effectiveness and efficiency of operations, that is having sound internal controls; second is the reliability of financial reporting, that is having transparency and good disclosure practices; and finally compliance with laws and regulations. Meeting these objectives will ensure that a company has key aspects of corporate governance, which are:

- Accountability to all stakeholders
- Transparency to all stakeholders
- Equality of treatment for all stakeholders

1. The Board of Directors

A decade back taking a directorship position in a company was considered to be a very honourable job but with very little effort or accountability. Today this job has become a very onerous job. One has to keep himself well informed about the affairs of the company as well as other regulatory aspects, should be very vigilant and should be able to ask the right kind of questions. The board is accountable to the company and the shareholders. Its prime responsibility is to provide strategic guidance to the management. It is also responsible for effective monitoring of the management. Specifically, the board should review and give guidance on the business plans of the company, evaluate and approve major capital expenditure decisions, acquisitions and divestitures, look into risk management and set performance objectives. It is also responsible for monitoring the effectiveness of company's governance practices and recommending changes as and when necessary.

The board should apply high ethical standards, take into account the interests of stakeholders and exercise objective independent judgment on corporate affairs. For performing these tasks, the board of directors should have optimum size and mix of directors. It should have both executive and independent directors; it should have directors with varied skills and experience. There should also be a policy of rotation of directors across committees so that they develop a broader perspective. For a board member to function effectively, it is important that he is fully informed. It is the responsibility of the management to provide all the information required by the board to function effectively. The board functions through various sub-committees, such as risk management committee, investor grievance committee, compensation committee and nomination committee. Effectiveness and independence of these committees is crucial for the board to function effectively.

2. Role of Management

Responsibility of ensuring sound corporate governance practices lies with the board of directors. However, top management is responsible for ensuring that the board gets the right information to act on. Specifically, the management has following roles and responsibilities with regard to corporate governance in a company:

- Financial reporting and certification to board of directors by chief financial officer and chief executive officer.
- Making sure that financial statements and cash flows present true and fair view and comply with accounting standards and applicable laws.

- Ensuring that no fraudulent, illegal or violative transaction is entered by the company.
- Responsibility for design and operations of effective internal controls.
- Disclosing deficiency in internal controls and steps taken for proper disclosure and transparency to stakeholders.
- Ensuring that there is a whistle-blower protection policy in place.

3. The Role of Audit Committee

Having an audit committee is mandatory for specified listed companies, as per Clause 49 of the listing agreement. Also, as per Section 292A of Companies Act, all public companies with paid-up capital of more than Rs. 5 crore should also have an audit committee. Audit committee is a subset of the board and has to be headed by an independent director. The management and the auditors must report to the audit committee and are required to assist the audit committee discharging its corporate governance functions.

The function of audit committee is to assess and review the financial reporting system to ensure that financial statements are correct, sufficient and credible. It is also meant to provide proper direction and oversee operations of total audit function. It is responsible for organisation, operation and quality control of internal audit and external audit and for reviewing adequacy of internal controls.

3.1 The role of external auditors

The objective of statutory audit is to have an independent examination of the books of account of the company and to provide opinion on true and fair view of financial statements. It is also to ensure the preparation of transparent accounts in accordance with the accepted accounting standards and practices. External auditors are required to follow the auditing standards issued by Institute of Chartered Accountants of India. Apart from these auditing standards, there are ethical standards which the external auditors must also address. An external auditor must ensure that his independence is not compromised in any way - for example, he cannot write the accounts of the company or be an internal auditor to a company where he is working as an external auditor.

Conclusion

The suggestions and views of the three speakers demonstrate three clear paths - self governance, the use of technology and the importance and role of audit which should help mitigate corporate governance challenges in India.

Author's Profile

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