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Asian Corporate Governance Association (ACGA)

## **“Corporate Governance in India”**

Presentation by:

Sharmila Gopinath, Research Director India, ACGA

Taiwan Corporate Governance Association, Taipei

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# Agenda

1. “CG Watch 2014”: ranking 11 Asian markets
2. India Today
3. Boards and its committees
4. Directors: training and accountability
5. Bank Governance
6. Conclusion

# 1. CG Watch 2014: Market rankings

CG Watch market scores: 2010 to 2014					
(%)	2010	2012	2014	Change 2012 vs 2014 (ppt)	Trend of CG reform
<b>1. = Hong Kong</b>	65	66	<b>65</b>	(-1)	Weak leadership, tough enforcement
<b>1. = Singapore</b>	67	69	<b>64</b>	(-5)	International vs local contrast continues
<b>3. Japan</b>	57	55	<b>60</b>	(+5)	Landmark changes, can they be sustained?
<b>4. = Thailand</b>	55	58	<b>58</b>	-	Improving, but new legislation needed
<b>4. = Malaysia</b>	52	55	<b>58</b>	(+3)	Improving, but still too top-down
<b>6. Taiwan</b>	55	53	<b>56</b>	(+3)	Bold policy moves, can they be sustained?
<b>7. India</b>	48	51	<b>54</b>	(+3)	Bouncing back, Delhi more supportive
<b>8. Korea</b>	45	49	<b>49</b>	-	Indifferent leader, more active regulators
<b>9. China</b>	49	45	<b>45</b>	-	Focus on SOE reform, enforcement
<b>10. = Philippines</b>	37	41	<b>40</b>	(-1)	Slow reform, improved company reporting
<b>10. = Indonesia</b>	40	37	<b>39</b>	(+2)	Big ambitions, can they be achieved?

Source: Asian Corporate Governance Association

# Overview of 11 Asian markets: 2014 vs 2012

- **Hong Kong and Singapore:** Equal first, but on lower scores.
  - Regulatory conflicts of interest, out-of-date institutional structures, opposition to reform, and many other factors.
- **Middle markets:** More cause for hope -
  - **Thailand:** No fall in score – a good result. Drops to equal fourth.
  - **Japan:** Leapt into third (again).
  - **Malaysia:** Continues to improve. Higher score, same ranking.
  - **Taiwan and India:** Higher scores, same ranking.
- **Korea and China:** Same score, same ranking.
  - Some improvements in their CG, but losing ground as regional benchmarks rise, hence scores stay the same.
- **Philippines and Indonesia:** Former falls, latter rises, equal last.

# The rising middle

## Japan, Thailand, Malaysia, Taiwan and India

### The view from the middle of our survey is considerably more uplifting.

- These five markets are the most motivated to achieve higher scores.
- Concerted effort to strengthen CG policies and regulations
  - **Japan and Taiwan** - major new CG policy initiatives, better enforcement. Some basic rules still weak, though, in disclosure and shareholder rights.
  - **Thailand and Malaysia** - moving ahead with pre-existing national CG policies and plans. Enforcement also better. But Political / Regulatory falls in Thailand. And Malaysia reluctant to make some obvious rule changes (eg, poll voting).
  - **India** – a landmark new company law, improved listing rules, better enforcement.
- Higher enforcement scores mostly due to the efforts of regulators.

## 2. India Today

The new Companies Act 2013, a simplified listing agreement and other rules in the past three years have brought about a lot of changes:

### ■ **Related-party transactions:**

- First time India has related-party transaction rules.
- RPT rules in the Act already diluted, citing ease of doing business.
- SEBI was pressured to align its rules, but securities laws should be more stringent.
- But SEBI continues to insist related and interested parties cannot vote.

### ■ **Gender equality in the boardroom:**

- First time any regulator has mandated at least one woman director on the board of all listed companies.
- Meaningless if promoters merely add their relatives or close associates.

### ■ **Voting by poll:**

- India managed to get voting by poll in through the back door, through mandatory e-voting.

# Laws, rules and regulations cont'd

## ■ CSR:

- 'Mandatory' CSR activities for certain classes of companies.
- An issue for many institutional investors is CSR being seen as philanthropy rather than strategic CSR.

## ■ Disclosure requirements:

- Continuous disclosure requirements overhauled by SEBI.
- Materiality events finally defined.
- Modified disclosure rules for mutual funds, a positive reform on stewardship. Mutual funds need to include their rationale for their voting decisions.

## ■ New insider trading regulations:

- No trading when in possession of price sensitive information, except off-market inter-se transfers between promoters; trade must be pursuant to a trading plan.
- Challenge is that anyone can be an insider who is in regular touch with the company, e.g. its law firm or auditors or analysts.

# 3. Boards and its Committees

## ■ **Boards and its committees:**

- Companies Act 2013 requires board to have audit committee; nomination and remuneration committee; Stakeholders' relationship committee; and corporate social responsibility committee.

## ■ **Audit Committee:**

- Minimum 3 directors, with majority independent.
- For a listed company, as per SEBI's Clause 49, chairman is independent and must be financially literate.

## ■ **Nomination and Remuneration Committee:**

- Minimum 3 directors, half must be independent and chairperson must be independent, according to Listing Agreement.

## ■ **Stakeholders Relationship Committee:**

- Non-executive director as chairperson and any other members that board sees fit.

# Boards and Committees

## ■ Risk Management Committee:

- SEBI requires this committee to be formed with majority of members to be board members although senior executives can also be on the committee.

## ■ Corporate Social Responsibility Committee:

- Three or more directors with one as an independent director.

## ■ Diversity on Boards:

- As mentioned earlier, one woman director on a company's board.
- Today, due to cross-border operations, a number of companies are “globalising” their boards: Infosys, Vedanta.

# Directors: training and accountability

## ■ **Code for independent directors:**

- A code of conduct for IDs and non-executives provides outline of professional conduct, role and functions, duties and the manner of appointment and reappointment of IDs.
- Cannot hold office for more than two consecutive five-year terms.
- To hold one meeting a year without non-independent directors or company management

## ■ **Evaluating the board and its directors:**

- Companies Act mandates a board to have a formal annual evaluation of itself, its committees and the individual directors, which must be reported in the directors report.

## ■ **Training:**

- SEBI mandated training for IDs in its listing agreement – a first, while Companies Act talks of “regularly” updating and refreshing their skills.
- Board training and evaluation has become big business: IoD, private firms, accounting firms, industry associations.
- But directors, especially big name industrialists, do not feel the need for training – “I know what I am doing”.

# Directors, training and accountability cont'd

## ■ **Accountability:**

- Companies Act spells out liabilities for directors that fail their duties.
- Today, independent directors will be held liable for “acts of omission or commission by the company” that occurred through board processes and he had knowledge of them.

# Bank Governance

State-owned banks are suffering due to a combination of inefficiency, corruption at certain levels and bad risk management and internal controls:

- **Non-performing assets have skyrocketed at state-owned banks:**

- The Reserve Bank of India governor, Dr. Raghuram Rajan, told banks to clean up their balance sheets by March 2017.
- Central Bureau of Intelligence has named five current and former executives in its report into IDBI's US\$142.5 million loan to Kingfisher Airlines.

- **Lack of governance:**

- In May 2014, the Nayak Committee published a report skewering PSUs and the government for inefficiency and lack of governance, proposing various remedies.
- In the 2015 Budget Speech, a 7-point plan, incorporating the recommendations was proposed. Since then a bank board bureau to help in selecting heads of PSUs has been set up and a holding company to hold the government's shares in banks is proposed.

# Conclusion

- Corporate governance is not just dependent on companies and its executives, boards, committees, investors must do their part.
- Institutional investors are now a lot more vocal because of SEBI requiring mutual funds to vote their shares and provide their reasoning for their votes.
- Corruption is an issue, but one that is being addressed.

# Contact Details

Sharmila Gopinath  
Research Director India

Asian Corporate Governance Association Ltd

Room 1801, 18<sup>th</sup> Floor, Wilson House  
19-27 Wyndham Street, Central, Hong Kong

Tel: 91-9846513987  
Email: [sharmila@acga-asia.org](mailto:sharmila@acga-asia.org)  
Website: [www.acga-asia.org](http://www.acga-asia.org)