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Asian Corporate Governance Association (ACGA)

# "Corporate Governance in India"

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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 |
|---|---|---|---|---|---|
| **1. = Hong Kong** | 65 | 66 | **65** | (-1) | Weak leadership, tough enforcement |
| **1. = Singapore** | 67 | 69 | **64** | (-5) | International vs local contrast continues |
| **3. Japan** | 57 | 55 | **60** | (+5) | Landmark changes, can they be sustained? |
| **4. = Thailand** | 55 | 58 | **58** | - | Improving, but new legislation needed |
| **4. = Malaysia** | 52 | 55 | **58** | (+3) | Improving, but still too top-down |
| **6. Taiwan** | 55 | 53 | **56** | (+3) | Bold policy moves, can they be sustained? |
| **7. India** | 48 | 51 | **54** | (+3) | Bouncing back, Delhi more supportive |
| **8. Korea** | 45 | 49 | **49** | - | Indifferent leader, more active regulators |
| **9. China** | 49 | 45 | **45** | - | Focus on SOE reform, enforcement |
| **10. = Philippines** | 37 | 41 | **40** | (-1) | Slow reform, improved company reporting |
| **10. = Indonesia** | 40 | 37 | **39** | (+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  - Regulatory conflicts of interest, out-of-date institutional structures, opposition to reform, and many other factors.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.

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