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"CORPORATE GOVERNANCE WITH SPECIAL REFERENCE TO COMPANIES ACT, 2013."

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I. ABSTRACT:

"The word corporate or corporation is the English translation of the Latin term "corpus", which meant for "body". Governance stands for the process of administration by which the expectations of the persons with the legitimate interest to the company are required to be fulfilled. When these two words are associated to each other, it implies for the proper arrangement of the policies, frameworks, methods and practices by which the corporate undertake to maintain the transparency and the legitimate interests of the parties. The corporate governance in India has frameworks to provide the measures for accountability of management and the transparency in the company's way of work.

This article is related focuses on the history of corporate governance and its recognition in the Companies Act 2013."

II. INTRODUCTION:

The corporate governance is implied for the management of the business in a responsible manner with committed ethics and to maintain the transparency by which the confidence of all the related and interested parties can be sustained. The Companies Act, 2013¹, passed by the parliament open the new company law regime in India which replaces the more than 50-year-old law of company (the Companies Act, 1956). The present Act² seeks to provide more

¹ Act No. 18 of 2013.

² Ibid.

transparency and enhanced mechanism for the management of corporate affairs. The Act³ aims to facilitate good governance by placing the burden on the *Independent Directors (hereinafter referred to as ID)* to oversight the functioning of the board. The term Corporate Governance wins more importance when the high-profile fraud of the corporate world is being investigated and the reasons behind these frauds come in the form of inadequate corporate governance.

Now the application of word the corporate governance meant for the relationship between the management of the companies and stakeholders of it. The rules and the procedures that regulate the management and operate and control the business are referred to as corporate governance. The good corporate governance possesses many main features such as corporate structure's transparency, management's accountability towards the stakeholders of its company and the most important thing, the responsibility towards its stakeholders.

III. CORPORATE GOVERNANCE: AN OVERVIEW:

Cadbury Reports' (*The committee was headed by Sir Adrian Cadbury*) definition of the corporate governance is widely accepted and states that "Corporate governance is the system by which companies are directed and controlled. The boards of directors are responsible for the governance of their companies. The shareholder's role in governance is to appoint the directors and the auditors to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board's actions are subject to laws, regulations and the shareholders in general meeting"⁴.

The N.R. Murthy committee constituted by the SEBI in 2003 also given the definition for the corporate governance in the following words:

"Corporate Governance is the acceptance by management of the inalienable rights of shareholders as the true owners of the corporation and of their own role as trustees on behalf

³Id.

⁴ "Cadbury Report, European Corporate Governance Institute", available at: <https://ecgi.global/sites/default/files/codes/documents/cadbury.pdf> (last visited on December 11, 2019).

of the shareholders. It is about commitment to values, about ethical business conduct and about making a distinction between personal and corporate funds in the management of a company”⁵.

“Corporate Governance is the application of best Management practices, Compliance of law in true letter and spirit and adherence to ethical standards for Effective Management and distribution of wealth and discharge of social responsibility for sustainable development of all stakeholders”⁶.

IV. HISTORICAL BACKGROUND:

If we go through the history of the corporate world, we will find that it is full of several fraud and scams. After the study of it, we found that the existing rules and regulations were not adequate. There was a need for a law that can regulate and penalize the defaulters and encourage the key personnel who follow the regulations. After the investigation of the number of frauds and scandals came into the corporate world, the regulatory bodies are in a position to highlight failure which allowed the various companies to allow the illegal withdrawal of money that should have been used for the business purposes.

The lack of regulatory measures on the part of the various authorities in corporate failures is the reasons for the establishment of the *Committee of Sponsoring Organizations (hereinafter referred to as COSO)*. The various committees on corporate governance had studied the problems of the corporate world and given the various solutions to the management of the corporations. Sarbanes-Oxley Act of 2002⁷, was an attempt to resolve the issues related to corporate failure and to provide good governance regime, further to re-establish the faith of the investors. The Act⁸ had various provisions which reformulate the obligations of the corporate directors and other officers of the public companies. The most

⁵ “Report of N.R. Narayana Murthy Committee on Corporate Governance (2003)”, available at: https://www.sebi.gov.in/reports/reports/mar-2003/the-report-of-shri-n-r-narayana-murthy-committee-on-corporate-governance-for-public-comments-_12986.html (last visited on December 11, 2019).

⁶ ICSI Definition of Corporate Governance.

⁷ “An Act to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws, and for other purposes”, 107th of US Congress.

⁸ Ibid.

significant provision of the Act⁹ is that it fixes the responsibility on the company's senior officers for corporate failure.

V. DEVELOPMENT OF CORPORATE GOVERNANCE IN INDIA:

In 1990's *CII (Confederation of Indian Industry)* made the very first effort in corporate governance' field. It was a voluntary step taken by the Indian companies to enhance transparency and to gain the faith of the various stakeholders of the companies. These steps are derived to make the fairness in decision, accountability, transparency and responsibility of the companies towards the stakeholders.

The second step was taken by the *Security Exchange Board of India (hereinafter referred as SEBI)* in the form of Clause 49 of the listing agreement. The third major step was the constitution of the Naresh Chandra Committee and Narayana Murthy Committee, which were formed for the study of the company's corporate governance working model from the stakeholders' point of view. These committees in their reports recommended for differentiation of responsibilities and obligations of the management for good corporate governance.

"The Corporate Governance Voluntary Guidelines 2009"¹⁰ was published by the *Ministry of Corporate Affairs (hereinafter referred to as MCA)* to enhance the good governance in the companies' working styles. In this guideline the suggestions made regarding the rotation of the auditors of the company, various disclosure party related transactions, policies regarding whistleblowers, etc.

This guideline was issued in recommendatory nature for the listed companies which were broadly divided into six chapters named as Board of directors, Responsibilities of the Board, Audit Committee of the Board, Auditors, Secretarial Audit, and Institution of mechanism for Whistle Blowing. Few companies working in India take these guidelines seriously but the

⁹Id.

¹⁰ "The Corporate Governance Voluntary Guidelines 2009", available at: https://www.mca.gov.in/Ministry/latestnews/CG_Voluntary_Guidelines_2009_24dec2009.pdf (last visited on December 11, 2019).

majority of the companies had not been actively pursuing the standards of corporate governance. The final step for the betterment of corporate governance can be said to the introduction of various provisions like independent directors, women directors, resident directors, corporate social responsibility and compulsory compliance of the Secretarial Standards issued by Institute of Company Secretaries of India, etc. in the Companies Act, 2013¹¹.

VI. RECOGNITION OF CORPORATE GOVERNANCE UNDER THE COMPANIES ACT, 2013:

The sea of changes in the new Act¹² made the way for the incorporation of corporate governance in our country. The Act¹³ made various provisions to enhance the corporate governance which has taken forward to SEBI's Clause 49 of listing agreement ahead and it is no longer available only to the listed companies but now also available to the non-listed companies. The new Act¹⁴ makes various key provisions which transformed the corporate world in a way that it can run the corporate machinery with the globalized corporate regime.

VI.I COMPOSITION OF BOARD:

There is three class of director mention in the Act¹⁵. The Act¹⁶ prescribed minimum 3 directors for public companies, 2 directors for private companies and 1 for One Person Company and a maximum number of the directors can be 15¹⁷. For more than 15 directors, the special resolution in this regard should be passed. Further minimum on women director is also compulsory.

VI.I.I WOMEN DIRECTOR:

Section 149(1) of the Act¹⁸ and Rule 3 of the Companies Rules¹⁹ prescribed at least One Women Director for all Listed Companies and Non-listed public companies that have at least Rs.100 crores paid-up share capital or Rs.300 crores turnover.

¹¹ Supra note 1.

¹² Ibid.

¹³ Id.

¹⁴ Id.

¹⁵ Id s. 149.

¹⁶ Supra note 1.

¹⁷ Id, s. 149(1).

¹⁸ Supra note 1.

¹⁹ Companies (Appointment and Qualification of Directors) Rules, 2014.

VI.I.II RESIDENT DIRECTOR:

Section 149(3) of the Act²⁰ says that Person who has stayed for a period of at least 182 days in India in the previous calendar would be known as resident director and minimum one resident director on the Board is compulsory.

VI.I.III INDEPENDENT DIRECTOR:

Section 149(4) of the Act²¹ prescribed reservation of a minimum of one-third of the Board of every listed company for independent directors. Further Rule 5 of the Companies Rules²² prescribes reservation for at least 2 (two) independent directors for public companies having Rupees one hundred million paid-up share capital or Rupees one billion turnover, having in the forms of aggregate, outstanding loans, debentures and deposits exceeding Rupees five hundred million.

Further Rule 5 of the Companies Rules²³ prescribed that an independent director shall possess appropriate skills, experience and knowledge in one or more fields of finance, law, management, sales, marketing, administration, research, corporate governance, technical operations or other disciplines related to the company's business. The latest notification issued by the MCA on October 22, 2019, makes provision that an independent director should have passed an online proficiency self-assessment test conducted by the "Indian Institute of Corporate Affairs at Manesar".

VI.II CONSTITUTION OF A NUMBER OF COMMITTEES:

VI.II.I AUDIT COMMITTEE:

Section 177 of the Act²⁴ provides that both private and public company have to constitute an Audit Committee that comprises minimum, three independent directors, in the board along

²⁰ Supra note 1.

²¹ Ibid.

²² Supra note 18.

²³ Ibid.

²⁴ Supra note 1.

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with the chairperson who is capable of reading and understanding the financial statement. Further Rule 6 of the Companies Rules²⁵ prescribed the companies that need to constitute the Audit Committee. All listed companies and all other public companies having at least Rs.10 Crores paid-up capital or public companies having at least Rs.100 Crores turnover should constitute the Audit Committee.

VI.II.II NOMINATION AND REMUNERATION COMMITTEE (NRC):

Section 178(1) of the Act²⁶ provides that every listed company should have formed NRC consisting of at least three non-executive directors and at least one half of it should be an independent director. Further Rule 6 of the Companies Rules²⁷ prescribed that the Public company having at least Rs.100 crores Paid-up capital; or which have, in aggregate, outstanding loans or borrowings or debentures or deposits exceeding Rs.50 Crores should also constitute the NRC.

Further Section 178(2) &(3) provides that the NRC shall identify the persons who are eligible for the post of directors and who are eligible for the appointment in senior management in accordance with the criteria laid down and recommend them to the Board for their appointment and removal and shall carry out evaluation of every director's performance.

VI.II.III STAKEHOLDER RELATIONSHIP COMMITTEE (SRC):

Section 178(5) of the Act²⁸ states that the Board of Directors of a company shall constitute an SRC comprising a chairperson who should be a non-executive director and other members as decided by the Board. The company which has more than one thousand shareholders, debenture-holders, deposit-holders and any other security holders at any time during a financial year should constitute an SRC.

Further Section 179(6) of the Act²⁹ provides that this SRC will also be responsible for resolving the grievances of security holders of the company.

²⁵ Companies (Meetings of Board and its powers) Rules, 2014.

²⁶ Supra note 1.

²⁷ Supra note 24.

²⁸ Supra note 1.

²⁹ Ibid.

VI.II.IV CORPORATE SOCIAL RESPONSIBILITY COMMITTEE:

Section 135(1) of the Act³⁰ prescribes constitution of CSR in every company that have a Net worth of at least rupees five hundred crores or Turnover of at least rupees one thousand crores or a net profit of at least rupees five crores during any financial year. CSR Committee of the Board should comprise of three or more directors, out of which one or more director should be an independent director. Further Section 135(3) of the Act³¹ provides that the CSR Committee shall:

- Formulate and recommend a CSR policy to the Board, the policy should indicate the activities to be undertaken by the company as specified in Schedule VII;
- Estimate and recommend the expenses incurred on the activities referred in the above clause; and
- Monitor the implementation of CSR Policy in the company from time to time.

VI.III INTERNAL AUDIT:

Section 138 of the Act³² mandated Internal Audit for certain class of companies for Internal. Further Rule 13 of the Companies Rules³³ provides that all the listed companies or all the non-listed companies having at least Rs.50 crores paid-up share capital, at least Rs.200 crores turnover in the last financial year, outstanding debts or borrowings from the banks or public financial institutions of Rs.100 crores or more should have mandatorily followed the provisions of Internal Audit.

VI.IV COMPLIANCE REPORT:

Section 134 of the Act³⁴ makes provisions for the compliance of the reports as mandatory duty on the part of Directors. The Report should state that directors should make the provisions for the establishment of a proper system to ensure compliance with the applicable laws and such

³⁰ Id.

³¹ Id.

³² Id.

³³ Companies (Accounts) Rules, 2014.

³⁴ Supra note 1.

system are working effectively. Section 205 of the Act³⁵ provides that the Company Secretary have to draft a report to the board about the fulfillment of the provisions of this Act, and the various rules made thereunder and other laws which are applicable to the company.

VI. V SERIOUS FRAUD INVESTIGATION OFFICE (SFIO):

Section 211 (1) of the Act³⁶ provides that the Central Government shall establish an office known as the Serious Fraud Investigation office having the duty to investigate fraud relating to Company. Further Section 212 of the Act³⁷ mandates SFIO to investigate the matters of the company on the basis of report forwarded by the Registrar or inspector under Section 208 where further investigation into the matters of the company is necessitated; on receiving of information about a special resolution passed by a company that its matters are required to be investigated; in the interest of public; or on request made by any Department of the Central Government or a State Government.

VII. CONCLUSION:

The Act³⁸ provides a comprehensive mechanism to strengthen corporate governance. The proper check and balance are provided in the form of the independent director to make sure that the powers cannot be exercised in such a manner to harm the stakeholders. The accountability of the directors is ensured. These changes are in the right way to run the company smoothly and in its stakeholders' interest. These all are welcomed moves in the global corporate era and they will make the soul of the corporate machinery more powerful by developing a responsible corporate regime which will establish the faith of the stakeholders.

³⁵ Ibid.

³⁶ Id.

³⁷ Id.

³⁸ Id.