

Codes, Conscience, and Corporate Character: Fostering a Culture of New Corporate Governance in Indian Organizations

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ABSTRACT

Corporate governance plays a crucial role in earning investors' trust and fostering capital market growth. This article examines the contemporary challenges of corporate governance in India and proposes plausible solutions. It highlights internal issues such as individualistic decision-making and poor adherence to external norms, offering recommendations to fortify legal and corporate frameworks and foster a sustainable governance culture.

The present article endeavors to scrutinize the challenges of corporate governance in the contemporary landscape of India and what are the plausible solutions to them.

The internal challenges of individuality and the failure to adhere to external norms have become a corporate endemic today. No sincere approach to check this menace has been actuated so far.

This article presents suggestions to enhance corporate governance standards. It is crucial not only in comprehending the challenges that the contemporary landscape brings but also for the imperative of fortifying the legal and corporate framework.

INTRODUCTION

Sam Altman, the co-founder and CEO of OpenAI, was recently ousted, prompting diverse speculations.¹ The reasons behind his removal remain elusive, with theories ranging from covert AI development to alleged inactivity. Amidst varied perspectives, the overlooked legal aspect involves scrutinizing how multinational corporations adhere to "Corporate Governance." The board's decision to dismiss the CEO underscores the significant influence it holds in decision-

¹ Ari Levy, Hayden Field, 'OpenAI brings Sam Altman back as CEO less than a week after he was fired by board' CNBC (22 November 2023).

making processes, raising questions about corporate governance dynamics. The incident illustrates a robust governance framework, where even a founder is not immune to oversight - a sharp contrast to Indian corporate practices where promoters often hold disproportionate sway.

Corporate governance via transparency and accountability upholds credibility to attract investments for profit optimization and realize the ambitions and preferences of promoters, shareholders, stakeholders, and society.²

This incident happened in the US, a foreign country. If that had happened in India, no board could fire a company's promoter/co-founder, the person who started the business. The OpenAI case has many elements, but it shows the board's authority and power in making decisions to improve "corporate governance" in the corporation. In contrast, while examining recent global shifts, particularly in Europe and the Middle East, it becomes evident that power dominance predominantly rests with directors, top-level managers, and executives. However, in countries like India, where the concept of "King's son will be the king" has been a tradition since ancient times, the newly established business empires continue to uphold this longstanding tradition. This practice directly or indirectly influences the image of their respective corporate kingdoms.

HISTORICAL BACKGROUND

The origins of good governance in India can be found in Chanakya's fourfold duties outlined in the third century B.C.³ In India, the demand for corporate governance emerged in the 1900s due to issues that corporations were already struggling with, including chronic capitalism, inadequate fiduciary responsibilities on the part of their boards of directors, poor disclosure norms and a lack of transparency. The corporate governance framework has evolved through enacting various acts framing various rules and regulations based on the principles of *Good Governance, Fairness, Accountability and Transparency*.

²OECD, 'G20/OECD Principles of Corporate Governance' (2015) <<https://www.oecd.org/daf/ca/Corporate-Governance-Principles-ENG.pdf>> accessed on 3 November 2023.

³ Prathama Banerjee, 'Chanakya/Kautilya: History, Philosophy, Theater and the Twentieth-century Political' (2012) 2(1), 24–51 <<https://doi.org/10.5406/historypresent.2.1.0024>> accessed 3 December 2023.

Over the past 75 years, Indian corporate laws have changed and developed. The Companies Act of 1913⁴ was superseded by the Companies Act of 1956.⁵ The 1990s economic policies expanded corporations' role in several business sectors, and the control and command-based economic model was shifted to an entrepreneurial one. The government has already implemented several measures to establish a robust framework for corporate governance. The Companies Act of 2013⁶ was culminating because of recommendations made by several committees, including the *Dr. JJ Irani Committee*,⁷ the *Naresh Chandra Committee*,⁸ the *Kumar Mangalam Birla Committee on Corporate Governance in 2009*,⁹ and the *Narayana Murthy Committee in 2003*.¹⁰

Several regulatory, statutory, and non-statutory entities were founded, such as the *Indian Institute of Corporate Affairs (IICA)*, the *Serious Fraud Investigation Office (SFIO)*, and the *National Foundation for Corporate Governance (NFCG)*. Despite their statutory mandates, many recent incidents as well as organizational reports show that most of these bodies are underpowered, under-resourced, and overstrained, operating in silos with inadequate operational structures and frameworks. These instances have necessitated fresh approaches tailored to contemporary economic and technological realities, rather than clinging to conventional socio-economic frameworks.

FROM PRINCIPLES TO PITFALLS: FACING THE FAULT LINES OF THE MODERN CORPORATE FRAMEWORK

Despite commendable efforts by regulatory bodies and reports in formulating robust corporate governance laws, the unfortunate reality in our nation is the lack of substantive implementation. Corporate governance challenges persist, varying across countries like the USA and the UK. Issues include inadequate law enforcement, limited female representation in leadership, and unethical practices by large corporations. Just as the COVID-19 virus has produced new variants,

⁴ The Companies Act 1913.

⁵ The Companies Act 1956.

⁶ The Companies Act 2013.

⁷ Dr. JJ Irani Committee, *Report on Company Law* (31 May, 2005).

⁸ The Naresh Chandra Committee, *Report on the CII Task Force on Corporate Governance* (November, 2009).

⁹ Shri Kumar Mangalam Birla, *Report of the Kumar Mangalam Birla Committee on Corporate Governance* (2009).

¹⁰ N.R. Narayana Murthy, *Report of the SEBI Committee on Corporate Governance* (8 February, 2003).

the adaptation of corporate governance has spawned contemporary challenges in the twenty-first century.

**POWER SHIFTS IN PIXELS: ADDRESSING MAJORITY SHAREHOLDER INFLUENCE IN THE
DIGITAL ERA**

The evolution of technology and the emergence of the digital economy have significantly transformed financial markets, corporations, and the global economy in the 21st century. Due to the pandemic, some digitalization measures were implemented out of necessity rather than strategy, which made them less subject to the strict regulatory scrutiny that would have been required under normal circumstances. This may have exacerbated security threats such as cyberattacks and fraud. However, the crisis also presented an opportunity to implement productivity-enhancing measures, as interim measures proved more effective than pre-pandemic norms. Notably, the widespread adoption of virtual general shareholder meetings can enhance shareholder participation and engagement and become a permanent aspect of corporate governance.

While digitalization has amplified the involvement of shareholders and stakeholders in corporate governance, India's situation deviates from the standard narrative. Unlike most Western economies, India faces a unique challenge where digital advancements are geared to bridge the "agency gap" between management and dispersed shareholders.¹¹ The crux of the issue is the overwhelming sway of majority shareholders who wield significant control over a company's resources, redirecting them to serve their interests. Consequently, the "agency gap" shifts the focus from traditional management-dispersed shareholder engagement to the fundamental disparity between majority shareholders and other stakeholders. Despite the potential for digital tools to enhance participation, addressing the influence of influential shareholders remains a vital element of effective corporate governance.

¹¹ Wylie Judith, Anne Marie Ward & Hamill Philip, *Agency and Corporate Governance* (Encyclopedia of Corporate Social Responsibility, 1st edn, 2013) pp 55-63.

INSIDE THE INNER CIRCLE: BOARDS IN PSU GIANTS VS. FAMILY-OWNED BUSINESS EMPIRES

All the listed companies must comply with the mandates of The Company Act, 2013, LODR Regulations,¹² and DPE guidelines,¹³ but the Public Sector Undertakings (PSUs) as well as Family-Owned Businesses have their unique issues. The PSUs owing the government have issues related to the appointment of directors and the diversity needed in the boardroom. No shareholders other than the government have a role in appointing the Executive Directors, Nominee Directors, and Independent Directors (IDs). The unidirectional selection process raises doubts about the necessary skill set. The 2007 guidelines from the Indian government have attempted to address concerns surrounding the composition of the Board of Directors, establishment of Audit Committees, roles and authority of said committees, subsidiary company issues, disclosure practices, accounting standards, risk management, compliance, and implementation schedules in public sector undertakings (PSUs). Despite these efforts, the Ministry of Public Enterprises reports that most PSUs need to improve their adherence to the regulations.

In addition, family-owned businesses have limited powers and autocratic leadership. Whether giants like Reliance, Tata, Godrej, and Times of India or smaller ventures, nearly 90% are family-owned. Due to this hierarchical structure, family members often become directors. This familial prioritization, termed parentalism, lacks democratic principles, sidelining directors in decision-making. The current situation poses a threat to minority shareholders while favoring the controlling family. The central question pertains to the intention of corporate governance i.e. restricting managerial autonomy and overseeing shareholders or pursuing the contrary. Thus, while compliance frameworks exist, actual governance outcomes are significantly influenced by entrenched institutional and familial structures.

CUSTODIANS OF FAIRNESS: THE ROLE OF PROXY FIRMS & INDEPENDENT DIRECTORS IN ENSURING FAIR CORPORATE GOVERNANCE

¹² Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Last amended on 23 October 2023).

¹³ Department of Public Enterprises, *Guidelines on Corporate Governance for Central Public Sector Enterprises* (May 2010).

Recently, the bid of Mr. Anant Ambani, the son of the business tycoon, Mukesh Ambani, to become a Director at Reliance Industries Ltd was opposed by two Proxy Firms - Institutional Investor Advisory Services India Ltd (IIAS) and Institutional Shareholder Services (ISS). These entities encouraged RIL shareholders to reject Anant's appointment while favoring Isha and Akash, his elder siblings, both aged 31 years, to join the RIL's board.¹⁴

This serves as a prime illustration of the role of proxy advisory firms in protecting shareholders' rights and interests through autonomous decision-making. These firms promote corporate governance by conducting comprehensive assessments of potential board members and designated auditors and offering impartial and unprejudiced counsel to shareholders. The Securities and Exchange Board of India (SEBI) strictly regulates these firms.

Another significant individual who can contribute to enhancing corporate governance is the Independent Director. However, recent trends indicate that independent directors are not particularly efficient in their roles. The appointment of independent directors and their decision-making powers are significantly influenced by promoters and the board of directors. Consequently, independent directors are unable to exercise their authority and every action they take is subject to the approval of the board of directors (via promoters).¹⁵

Both proxy advisory firms and independent directors must operate independently to ensure that their decision-making process is focused on the company's best interests and remains unaffected by external influences. If this scenario does not occur, and both the proxy consulting firms and independent directors are ineffective since they often face a situation of "conflict of loyalty" between legal duties and personal relationships, it could pose a substantial risk to the company's operations.

THE ESG IMPERATIVE- LONG-TERM SUSTAINABILITY OR FUTURE-READY?

The ongoing development has added a buzzword in corporate boardrooms- ESG, i.e., Environment Social Governance. While the SEBI has ordered the top 1,000 listed Indian

¹⁴ Hitesh Vyas, 'Proxy advisory firms oppose Anant's appointment on RIL board: What are these firms, and how should investors react?' *The Indian Express* (20 October 2023).

¹⁵ Stakeholders Empowerment Services, *Proxy Advisory Services* (43rd AGM, 2020).

entities by market value to disclose their ESG risks and responsibilities as well as their approach to mitigating the same in the Business Responsibility and Sustainability Reporting (BRSR) framework¹⁶, many corporate giants are considering this as a boardroom level discussion. This concept is familiar; it has recently been much cottoned under nine key performance indicators¹⁷. Its multifold benefits are very beneficial for the 3Ps of Sustainability¹⁸. Still, the companies are afraid of the growing pressure from the stakeholders concerning the ESG disclosures and high demands for traceability and transparency of business operations. The technological interventions in the form of the Internet of Things (IOTs), Artificial Intelligence (AI), and Digital twins have eased up the task of getting a better E performance, but what stand at the forefront is the following questions:

What data should be gathered? Who ought to participate in the procedure? Where is the information situated within the organization? Additionally, it is imperative to undertake the formidable task of crafting a reliable and resilient data collection system that can withstand the test of time.¹⁹

The continuous instances of greenwashing, prioritization of short-term financial gains over long-term gains, and the complexities of supply chains have vastly hindered the very purpose of this concept. The other concerns of the board include handling sensitive information, such as employee data or carbon emissions data, following privacy regulations. Ensuring compliance with data protection and privacy laws with 2.5 quintillion bytes of data produced daily,²⁰ such as the GDPR,²¹ while collecting, storing, and processing ESG data poses additional challenges. Making it a legal mandate won't suffice the cause; what must be done is inculcating the spirit of governance. There must be robust data management processes, standardized and compulsory ESG reporting frameworks, stakeholder engagement strategies, and compliance measures to attain the stage of a more comprehensive ESG framework.

¹⁶ Securities and Exchange Board of India, *Business Responsibility and Sustainability Reporting* (2012).

¹⁷ *ibid.*

¹⁸ Jeroen Kraaijenbrink, Forbes, *What are the 3Ps of the triple bottom line really mean?* (10th December, 2019).

¹⁹ Deloitte, *What are the challenges in ESG Reporting?* (2021).

²⁰ Bernand Marr, Forbes, *How much data do we create every day?* (2021).

²¹ General Data Protection Regulations 2016.

CONCLUSION

Corporate governance is paramount in ensuring transparency, accountability, and sustainability in business operations, along with playing a pivotal role in safeguarding the interests of shareholders, bolstering investor confidence, mitigating risk, adhering to regulations, and enhancing overall company performance. However, all stakeholders must take a collaborative approach to address the multifaceted issues and challenges confronting corporate governance in India.

Though the data shows that non-compliance with the norms of SEBI has decreased significantly, the other crucial aspects of corporate governance still need to be addressed. Although India has crafted corporate governance laws with an all-encompassing comprehension of worldwide governance standards, including those of the United States, there remains a necessity for more efficient avenues to assist policymakers in formulating corporate governance standards that are fitting for Indian conditions. In terms of the future trajectory, it remains to be ascertained whether the directives and actions will remain in their current state or undergo a transformation into a more formal and binding nature over time. Thus, in order to achieve our national development objectives, our goal must be to instill a governance ethos in our organizations that champions integrity and inclusivity, ensuring that Indian companies are not only future-compliant but also future-resilient.

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