

Corporate Disclosure: A Tool for Improving Corporate Governance Practices in India : An Empirical Analysis

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Corporate Governance is a phenomenon of assessing the fairness of conducting business by various corporations. Corporate Governance definition broadly stresses issues of transparency in the financial disclosures. The distribution of rights and responsibilities among board of directors, audit agencies and other stakeholders also have a direct bearing on the overall governance by the organizations. India, currently, has been inundated with heavy foreign direct investments (FDIs) in all sectors, it being the fastest growing economy. To maintain this momentum, a good governance mechanism is highly essential. The transparency and fairness in doing business is the key to good governance. Corporate Governance relies heavily on the mindset of the top hierarchy and its compliance certainly depends upon how the top management deals with various norms as mandated by the regulatory agency Securities & Exchange Board of India (SEBI). To develop a road map for mandatory compliance towards various norms, SEBI has mandated to include a separate chapter on Corporate Governance in the annual reports by the listed companies.

The present study attempts to understand the extent of compliance towards mandatory and non-mandatory norms as specified by SEBI. Thus, the study evaluates the Board Compositions, Role of Independent Directors, Role of Statutory and Non-Statutory Committees, and contribution of the companies towards Corporate Social Responsibility (CSR). The research is based on the analysis of the secondary data collected through 104 important parameters published in the annual reports of the listed companies for the year 2013-14. The research attempts to develop a scorecard based on the company's data for evaluating performance regarding corporate governance practices. It concludes with suggestions and measures for improving Corporate Governance regime in India.

Key Words: Corporate Governance; Foreign Direct Investments; Financial Disclosures, Corporate Social Responsibility.

Introduction

Corporate Governance is a system by which business corporations can be evaluated in terms of fairness and transparency in disclosing their financial results. Globally, the Corporate Governance regime, evolved two decades ago, has laid a framework to develop basic norms for governance. The contributions from Cadbury Committee, OECD (Organization for Economic Cooperation & Development), CII, and Kumara Mangalam Birla Committee etc., in this

regard are highly remarkable in devising a benchmark to embark upon for disclosures in the annual reports. OECD, aptly, defines Corporate Governance as a system by which business organizations are directed and controlled. The listing agreement contains a comprehensive list of various norms comprising of statutory and non-statutory parameters, that needing adherence by the listed companies. The market regulatory agency Securities & Exchange Board of India

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(SEBI) has evoked a mandatory compliance of corporate governance norms by the listed companies. The mechanism for good governance calls for honest and ethical compliance to different parameters, which is heavily dependent on organizational beliefs and culture and the mindset of the top order. Corporate Governance being, the most powerful control measure in assessing a firm needs to be legislated at the earliest.

It is highly assertive to note that companies with good governance practices ultimately achieve a sustainable competitive advantage and will survive in the long term. India, after the liberalization, has emerged as a favorite destination for foreign direct investments, joint ventures and strategic alliances. In view of such large-scale foreign investments, the concept of Corporate Governance needs to be strengthened sooner than later. SEBI has mandated that a separate chapter on corporate governance is included in the annual reports stating the compliance towards statutory and non- mandatory norms. It is worthwhile to examine the extent of compliance by the listed companies towards discretionary norms as companies generally overlook the compliance towards non-statutory ones. The current paper attempts to evaluate corporate governance norms in a descriptive manner. To begin with, the paper defines Corporate Governance, and subsequently examines the extent of compliance towards various norms as specified by SEBI, by the listed companies in their annual reports of 2013-14.

Review of Literature

Numerous studies all over the world have been carried out on the subject of Corporate Governance practices and a few of these, which are relevant to the subject, have been cited hereunder:

- Shukla (2014), concludes that CSR is a self regulating mechanism and in modern era there is a need to integrate CSR with global governance as a voluntary practice.
- Times of India; April 18, 2014; “137 top cos. need to change auditors; Have to find replacements by FY 18 to comply with new companies act”; The report is based on analysis done by shareholder proxy firm IIAS (Investor Advisory Services) shows that over half of the 221 companies studied have auditors whose tenure has exceeded 10 years. The recently notified section 139 of the Companies Act 2013 makes it mandatory for audit firms to be changed after every 10 years. The list of Companies with same auditors includes Hindalco with over 50 years, RIL with over 35 years.
- Mathur (2013) outlines reasons leading to failure of Corporate Governance in Banks.
- Varghese (2013) on the subject of “Corporate Disclosure by Indian Companies” has reported a significant difference between disclosure of Strategic Information (corporate strategy) & non strategic information on items disclosed in annual reports.
- Vasanthi , George (2013), indicates role of Chairperson in Women directors on board.
- The Tribune, 21st December, 2013; “New Corporate Governance Norms Soon”, says SEBI; Mr. UK Sinha, Chairman SEBI, that, of the listed companies, more than 1100 are non-compliant of clause 40A of the listing Agreement and over 900 firms don’t follow clause 49 dealing with corporate governance and board constitution.
- Varghese (2012), evaluates 160 Indian and Multinational companies on 154 parameters relating to mandatory disclosures in annual reports of 2001-02 to 2003-04 and reveals that only 41 parameters out of 154 disclosed by companies.
- Prasanna, P (2011), studied 100 listed companies out of 212, concludes significant correlation between Governance and organizational effectiveness.
- Srinivasan Padmini (2011), Status of Corporate Governance Research in India.
- Rudra Titus (2010), conducted study of 43 companies out of Fortune 500 most valuable companies. The companies were studied based on 32 parameters disclosed in the annual reports and suggests that firm level policy related to great transparency and disclosure is positively associated with foreign institutional investments.
- Garg M, Divya (2009), studied 200 companies of BSE and found that only 132 are providing annual reports on the websites, only 29 accounting standards as issued by ICAI have been examined. It concluded that 60% companies make 60% disclosures.
- Shukla (2008), studied annual reports of 130 listed companies for status of Corporate Governance Practices.
- Pithadia, V (2007), outlined the importance of corporate governance and its applicability in the Indian business enterprises.

Thus from the above review, it is evident that only few empirical analysis based studies to unearth the compliance of Corporate Governance practices across Indian boards have been conducted. The present study, thus, attempts to

analyze the item wise compliance, empirically, towards various corporate governance practices reported in the annual reports. The current study also makes an effort to rank the industry as well as individual company based on the score obtained on various items under different heads of Corporate Governance Practices.

Objectives

The major objectives for conducting this study are:

1. To study the disclosure of extent of compliance of various Corporate Governance Practices in the annual reports by the listed companies in respect of various parameters.
2. To assess the contribution made by the corporations towards Social responsibilities.
3. To rank Industries and Companies based on compliance scores obtained for CG practices

Research Methodology

Universe and Sampling Design of the Study

Out of the top 100 listed Indian companies with National Stock Exchange, classified broadly into ten sectors, including Public Sector Undertakings (PSUs') but excluding Insurance Sector companies, on the basis of market capitalization constitute the universe for the purpose of this study. Out of this universe, at least three companies from each sector have been selected to make a total of 30 companies which constitute the sample for the study purpose. An exploratory research based on secondary data in the published annual reports of these listed companies, assessed through company websites, for the year 2013-14, has been conducted. From the annual reports, 104 parameters have been identified for study, grouped under ten broad categories of Director Report, Board Composition, Board Meetings, and Non-mandatory requirements, Board Committees, Audit Committee, Remuneration Committee, Risk Management Committee, CSR Committee and Independent Auditor Report as per Table I:

*Each disclosed parameter has been assigned a score ranging from 1 to 3, depending upon the extent of compliance. The summated maximum score applicable to each company is 150 and thus each industry, comprising of three companies, will be ranked on the basis of actual scores against a maximum score of 450.

The overall industry average is 83.3% and the notable

industries scoring below the overall average include-Banking, Pharma, Metals and Capital Engineering. Among all industries, the FMCG sector comprising of companies ITC, Hindustan Unilever and Dabur India) ranks 1st, followed by Oil & Gas sector constituted of Oil & Natural Gas Corporation (ONGC), Reliance Industries, and Cairns India . The Cement industry at IIIrd, rank contains ACC, Ambuja Cement & Ultra Tech Cement, while the IT sector at IVth, rank is made up of companies such as TCS, Infosys and Wipro. The Vth, rank goes to Public Sector Undertakings (PSU) with companies as Coal India, NTPC and Oil India. The Automobile sector, with Tata Motors, Maruti Suzuki, and Hero Motor Corp, occupies VIth, rank followed by Capital Engineering Sector at VIIth, rank made up of L&T, BHEL & Siemens. The Metal industry with Tata Steel, Steel Authority of India (SAIL) & Hindalco at VIIIth rank while the Pharma sector is placed at IXth rank with companies Sun Pharma, Cipla & Ranbaxy Labs. The last in the ranking at Xth, place is Banking Sector comprising of HDFC Bank, State Bank of India and ICICI Bank.

Category wise Analysis

The category wise results at a glance are shown in Table 3 wherein each category has been ranked as per actual scores.

1. Director's Report

Under this category, twenty parameters, each carrying a score of one, have been studied. The average achievement is 95.2%, the largest among the other categories thus placing it at 1st rank as is evident from the table given hereunder.

2. Board Composition

This category evaluates in particular, the composition of the board with respect to total strength of directors comprising of Executive, Non-executive and Independent directors, Chairman of the board, appointment of woman director, director profiles and evaluation mechanism for Independent Directors. This analysis is based on 13 parameters with a maximum score of 25. The overall achievement under this category is 76% and is ranked VIIIth.

3. Board Meetings

This category contains nine parameters with a maximum score of 15 covering the number of board meetings, presence of Chairman in the board meetings as well as in the AGMs, lead independent director and meeting of independent directors without the presence of executive director. The achievement of 83.8% of this category places it at VIth rank.

4. Non- Mandatory requirements

This category evaluates ten discretionary parameters which include: insider trading, whistle blower policy, SCORES, and succession planning being highly important from the governance point of view. The overall achievement of 64% that places it at Xth rank is a testimony that companies pay scant attention to these parameters.

5. Board Committees

Only five types of committees comprising of mandatory Audit & Investor Grievance committee and non-mandatory committees such as Remuneration, Risk & Corporate social responsibility committees have been studied. This category has scored 87.3% and is ranked IVth.

6. Audit Committee

Perhaps the most vital organ of the organization, there is a fair justification to this category owing to 92% achievement and is ranked IInd^o among the ten categories. It is evident enough from the high achievement that all eight parameters are strictly adhered.

7. Remuneration Committee

The achievement of 79.3% (VIIth rank) of this non-mandatory norm, indicates that there is a need for better compliance by the companies under this category.

8. Investor Grievance Committee

The study of six parameters under this category has resulted in 86.7% achievement with Vth rank suggests fair compliance towards this issue.

9. Corporate Social Responsibility Committee

The second in the worst performer's category is this category where a meager 64.7% achievement is shown indicating that the companies will have to be more liberal in undertaking the social issues. The company's act has now made it compulsory for the corporations to spend a minimum of 2% of their net profits on CSR initiatives thus; there is every likelihood that by next year the scores will improve.

10. Independent Auditor Report

The overall achievement in this category is 90.5% and ranks IIIrd^o. Out of ten sectors, nine have achieved 100% compliance towards twenty parameters under this category; except for the Banking sector. The banking sector follows entirely different set of norms for auditing which do not match the traditional norms followed by other sectors.

Conclusion and Suggestions:

1. The individual ranking of each company based on the actual score is as given in Table 4.
2. The best compliance comes from sectors of FMCG, Oil & Gas followed by Cement.
3. The sectors of Capital Engineering, Metals, Pharma and Banking post average compliance.
4. Woman Directors on Board of Directors are limited to only few companies and now that SEBI has made it mandatory to have a woman director, it will be interesting to review the annual reports of the subsequent financial years.
5. The other area of concern is Succession Planning where the score is very low.
6. Except WIPRO, Reliance, NHPC & Dr Reddy no other company has designated an Ombudsman to look into and settle issues concerning Insider trading, frauds etc.

Future Study

The new company's Act 2013 has laid down certain additional criteria for the listed companies for compliance towards corporate governance norms hence a fresh review based on the disclosures contained in the annual reports of 2014-15 must be carried out to explore the adherence to such amended norms. The concept of appointing a woman director on board is gaining prominence and all listed companies are required to have a woman director by the end of current financial year 2015-16, thus, further study is required.

The CSR spend of 2% of the net profits as mandated under new company's act needs to be probed to check if companies are fulfilling their social obligations in the right perspective.

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ANNEXURE

Table 1 : Category wise Scores

SN	Category	Parameters	Max Score
1	Director Report	20	20
2	Board Composition	13	25
3	Board Meetings	9	15
4	Non Mandatory Requirements	10	10
5	Board Committees	5	5
6	Audit Committee	8	20
7	Remuneration Committee	9	15
8	Investor Grievance Committee	6	10
9	CSR Committee	4	10
10	Independent Auditor Report	20	20
	Total	104	150

Research Findings : The following table 2 indicates Industry wise achievement

Table 2 : Industry wise Score/ Ranking

SN	Industry	Actual Score	Max Score	%	Rank
1	FMCG	399	450	88.7	I
2	Oil & Gas	390	450	86.7	II
3	Cement	389	450	86.4	III
4	IT	387	450	86.0	IV
5	PSU	385	450	85.5	V
6	Automobile	375	450	83.3	VI
7	Capital Engg	372	450	82.7	VII
8	Metals	364	450	80.1	VIII
9	Pharma	352	450	78.2	IX
10	Banking	334	450	74.2	X
	Total	3747	4500	83.3	

Table 3 : Industry-wise/Category wise Rankings based on Compliance Scores

SN	Industry	1		2		3		4		5	
		Director Report		Board Composition		Board Meetings		Non Mandatory		Board Committees	
		%	Rank	%	Rank	%	Rank	%	Rank	%	Rank
1	Automobile	93.3	IV	76.0	V	82.2	III	60.0	IV	93.3	II
2	Banking	95.0	III	77.3	IV	88.9	I	63.3	III	93.3	II
3	Capital Engg	95.0	III	76.0	V	82.2	III	50.0	VII	100.0	I
4	Cement	96.7	II	81.3	I	80.0	IV	60.0	IV	86.7	III
5	FMCG	98.7	I	80.0	II	86.7	II	66.7	II	100.0	I
6	IT	98.7	I	77.3	IV	88.9	I	76.7	I	86.7	III
7	Metals	93.3	IV	78.7	III	82.2	III	56.7	V	66.7	IV
8	Oil & Gas	98.7	I	69.3	VI	86.7	II	76.7	I	93.3	II
9	Pharma	95.0	III	65.3	VII	77.8	V	53.3	VI	60.0	V
10	PSU	93.3	IV	78.7	III	82.2	III	76.7	I	93.3	II
Total/Rank		95.2	I	76.0	VIII	83.8	VI	64.0	X	87.3	IV
SN	Industry	6		7		8		9		10	
		Audit Committee		Remuneration Committee		Investor Grievance Committee		CSR Committee		Independent Auditor Report	
		%	Rank	%	Rank	%	Rank	%	Rank	%	Rank
1	Automobile	91.7	IV	86.7	II	73.3	VI	56.7	V	100.0	I
2	Banking	86.7	VI	91.1	I	96.7	I	70.0	III	5.0	II
3	Capital Eng	85.0	VII	75.5	IV	86.7	IV	66.7	IV	100.0	I
4	Cement	90.0	V	91.1	I	90.0	III	70.0	III	100.0	I
5	FMCG	93.3	III	91.1	I	86.7	IV	80.0	I	100.0	I
6	IT	95.0	II	84.4	III	83.3	V	50.0	VI	100.0	I
7	Metals	98.3	I	66.7	V	73.3	VI	46.7	VII	100.0	I
8	Oil & Gas	93.3	III	84.4	III	90.0	III	76.7	II	100.0	I
9	Pharma	83.3	VIII	62.2	VI	93.3	II	50.0	VI	100.0	I
10	PSU	95.0	II	60.0	VII	93.3	II	80.0	I	100.0	I
Total/Rank		92.0	II	79.3	VII	86.7	V	64.7	IX	90.5	III

Table 4 : Company wise Rankings

Rank	Company	%
I	ITC, Coal India	91.3
II	Ambuja Cement	90.0
III	Tata Motors	88.7
IV	HUL, WIPRO, ONGC, Reliance Ind	88.0
V	ACC, Dabur, Oil India	86.7
VI	L&T, TCS, NTPC	85.3
VII	Infosys, Tata Steel	84.7
VIII	Cairns India	84.0
IX	Maruti Suzuki, Ranbaxy Labs	83.3
X	Ultra Tech Cement	82.7
XI	Siemens India	82.0
XII	BHEL, Hindalco	80.7
XIII	Hero Motor Corp	78.0
XIV	SAIL	77.3
XV	HDFC Bank, Sun Pharma	76.0
XVI	Cipla	75.3
XVII	ICICI Bank	74.0
XVIII	State Bank of India	72.7

Table 5 : Industry wise / Category wise Scores

Category	1	2	3	4	5	6	7	8	9	10				
Industry	Director Report	Board Structure	Board Meetings	Non Mandatory	Board Committees	Audit Committee	Remuneration	Investor Grievance	CSR	Independent Auditor	Actual Score	Total Score	%	Rank
Auto	56	57	37	18	14	55	39	22	17	60	375	450	83.3	VI
Banks	57	58	40	19	14	52	41	29	21	3	334	450	74.2	X
Capital	57	57	37	15	15	51	34	26	20	60	372	450	82.7	VII
Cement	58	61	36	18	13	54	41	27	21	60	389	450	86.4	III
FMCG	58	60	39	20	15	56	41	26	24	60	399	450	88.7	I
IT	58	58	40	23	13	57	38	25	15	60	387	450	86.0	IV
Metals	56	59	37	17	10	59	30	22	14	60	364	450	80.1	VIII
Oil/Gas	58	52	39	23	14	56	38	27	23	60	390	450	86.7	II
Pharma	57	49	35	16	9	55	28	28	15	60	352	450	88.2	IX
PSU	56	59	37	23	14	57	27	28	24	60	385	450	85.5	V
Actual	571	570	377	192	131	552	357	260	194	543	3747	4500	83.3	
Total	600	750	450	300	150	600	450	300	300	600	4500			
%	95.2	76.0	83.8	64.0	87.3	92.0	79.3	86.7	64.7	90.5	83.3			
Rank	I	VIII	VI	X	IV	II	VII	V	IX	III				