

## AN ANALYSIS OF PROVISIONS IN COMPANIES ACT 2013 TO IMPROVE CORPORATE GOVERNANCE

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### ABSTRACT

The Companies Act 2013 which will be replacing the age old Companies Act 1956 once all its provisions are notified is aimed at ensuring higher standards of transparency and accountability, and seek to align the corporate governance practices in India with global best practices. In order to address the corporate governance requirements in unlisted companies which are more in number, a number of provisions are incorporated in the Companies Act 2013. The listed companies in India are obliged to comply with a more stringent requirement as provided under the listing agreement especially clause 49 of the stock exchange listing agreement. Apart from the provisions under the listing agreement, the listed companies have to comply with a number of regulations promulgated by Securities and Exchange Board of India (SEBI) under the SEBI Act. However, unlisted companies unless it is a material subsidiary of a listed company do not have to comply with any of the SEBI Regulations or listing agreement.

There is a host of public limited companies and private companies which are very large in size with substantial exposure to public due the nature of their business. Apart from this most of the companies in India both public and private depends largely on bank borrowings. Taking into account the fact that healthy banking sector is an essential element of the overall ecosystem of the country's economy, it is important to ensure that the companies which have large exposure to bank borrowings are managed in a prudent manner and follow sound corporate governance practices. This paper makes an attempt to study various provisions in the Companies Act 2013 incorporated with a view to implement and improve the corporate governance practices generally in companies in India as the corporate governance provisions in the listing agreement are applicable only to listed companies. Under the Companies Act 2013, companies fulfilling certain conditions are required to comply with the provisions related to corporate governance. The objective behind this is to protect interest of other stakeholders including those of minority shareholders and the Government. The required information is gathered mostly from the Companies Act 2013 and the ruled framed there under.

### INTRODUCTION

Adrian Cadbury, whose report has become the Bible of Corporate Governance, defines Corporate Governance as 'a system or process by which companies are directed and controlled.' Corporate Governance is a process or a set of systems and processes to ensure that a company is managed to suit the best interests of all stakeholders. Corporate Governance is concerned with the establishment of a system whereby the Directors are entrusted with the responsibilities and duties in relation to the direction of corporate affairs. It is concerned with the morals, ethics, values, parameters, conduct and behavior of the company and its management.

Good governance is primarily about values rather than rules. Corporate governance is defined as the set of systems, processes and principles by which a company is governed. They provide the basic framework and guidelines as to how the company can fulfill its goals and objectives in a manner that adds to the value of the company and is also beneficial for all stakeholders, including everyone ranging from the Board of Directors, Management, Shareholders, Employees, customers and society, in the long term.

Fredric Neuberger and Adam Demb in “The Legitimate Corporation” identify six groups of commonly distinguishable stakeholder, viz:

- Providers of funds – Shareholders
- Employees
- General Public
- Government
- Customers
- Suppliers

### **The Companies Act 2013 and Corporate Governance**

Corporate administration has been a subject of hot verbal confrontation in created nations like United Kingdom and Unites States throughout the previous two decades. With the opening up of economies, it has additionally been a worry for creating nation like India. The extension and importance of corporate administration in India expanded sizeably in the current time frame, especially taking after the budgetary division changes. As Indian corporates are finding new space in residential and worldwide markets for business development, their collaboration with the money related markets and contributing group too saw noteworthy surge. In this procedure, corporate administration came as a successful instrument for organizations to speak with the different sorts of partners by and large and financial specialists specifically.

Progression of the Indian economy started in 1991. From that point forward, there have been significant changes in both laws and controls in the corporate administration scene. A portion of the critical improvements which have bearing on presentation of Corporate Governance standards in India are given beneath:

- The most vital improvement in the field of corporate administration and financial specialist insurance has been the foundation of the Securities and Exchange Board of India (SEBI) in 1992. It has assumed a pivotal part in setting up the fundamental least standard procedures of corporate lead in India.
- The next noteworthy occasion was the Confederation of Indian Industry (CII) Code for Desirable Corporate Governance created by a board of trustees led by Mr.Rahul Bajaj The advisory group was shaped in1996 and presented it's suggestion in April 1998.
- Later two more boards were constituted by SEBI, one led by Mr.Kumar Mangalam Birla and the other by Mr.Narayana Murthy. The Birla advisory group presented its provide details regarding mid 2000 and the second council presented its investigate 2003.The proposal of these two boards of trustees had been instrumental in acquiring significant changes the corporate administration through the definition of Clause 49 of the Listing

Agreement.

- Along with SEBI, the Department of Company Affairs and the Ministry of Finance, Government of India, likewise took a few activities for enhancing corporate administration in India. For instance, the foundation of a review gathering to operationalize the Birla Committee proposals in 2000, the Naresh Chandra Committee on Corporate Audit and Governance in 2002 and the Expert Committee on Corporate Law (J.J. Irani Committee) in late 2004.
- SEBI executed the suggestions of the Birla Committee through the authorization of Clause 49 of the Listing assertion. Proviso 49, can be alluded to as a turning point as for the progressions in corporate administration in India. It is like Sarbanes - Oxley Act (SOX) in U.S.

Clause 49 extensively covers the accompanying matters as significant consistence prerequisites:

- Composition of the leading group of the chiefs
- Composition and Functioning of the Audit Committee.
- Governance and exposures with respect to backup organizations.
- Disclosures by the organization.
- CEO/CFO confirmation of the money related outcomes.
- Reporting on corporate administration as a component of the yearly report.
- Certification of consistence of an organization with the arrangements of Clause 49.

Great corporate administration may not be the motor of monetary development, but rather it is fundamental for the best possible working of the motor. Great corporate-administration practices can help expand speculation, diminish defilement, and lessen squandering of rare assets. The Companies Act 2013 looks to build up another benchmark for corporate administration in contrast with the past system under the Companies Act 1956.

The accompanying are the imperative arrangements fused under the Companies Act 2013 to address the hole in the recent Companies Act 1956 and enhance the corporate administration system. How these arrangements are relied upon to change the administration system for the most part taken after by organizations particularly unlisted organizations in India are additionally dissected?

- Independent Directors:- The recent organizations act 1956 did not contain any arrangements in regard of Board Composition like what is recommended under the Clause 49 of the posting understanding. However the organizations Act 2013 joined arrangements under area 149 which manages the prerequisite of specific organizations to have Independent Directors. According to the guidelines recommended under this Section, aside from recorded organizations the accompanying organizations is required to have Independent Directors on its Board
- Public organizations having paid up offer capital of Rs.100 crore or more; or

- Public organizations having turnover of Rs.300 crore or more
- Public organizations which have, in total, exceptional credits or borrowings or debentures or stores, surpassing Rs. 200 crore

The primary target of the above arrangement identified with Independent Directors is to guarantee that there is some kind of observing on organizations where the general population premium is included whether because of its size of business or its presentation to the banks by method for sizeable acquiring.

Code of Conduct for Independent Directors: - Schedule IV of the Companies Act 2013 prescribes a code of conduct to be followed by the Independent Directors. The aim of this is to establish more accountability and clarity on the role of an Independent Director. There are provisions which limit the liability of an Independent Directors and also distinguish the liability of an Independent Directors and non-executive director from the rest of the Board.

- Women Director:- The Companies Act 2013 prescribe all listed companies and certain other prescribed companies to have a women director on its Board. This measure is seen as a step to increase the participation of women in the management of companies.
- Duties of Directors:- Section 166 of the Companies Act 2013 prescribed the Duties of a Director. This helps directors to have more clarity on their duties and responsibilities at the same time bring more accountability to their actions.
- Related Party Transaction: - Section 188 of the Act deals with related party transactions. Taking into account the fact that related party transactions is one of the areas which are exploited and abused by the majority shareholder, the Government wants to ensure that there are some safeguards which prevent or minimize the level unfair related party transactions.
- Audit Committee:- Even though the erstwhile companies act 1956 provided for constitution of Audit Committee by certain companies, Section 177 of the Companies Act 2013 incorporated more detailed provisions related to Audit Committee including its constitution, terms of reference, power etc.,. The monitoring of the vigil mechanism envisaged under Act also brought under the Audit Committee. Considering that majority of members in the Audit Committee consist of Independent Directors, it is expected that the Audit Committee will play a critical role in the proper governance of all companies hereafter.
- Nomination and Remuneration Committee and Stakeholders Relationship Committee:- Section 178 of the Companies Act 2013 deals with Nomination and Remuneration Committee wherein it is mandatory for all listed companies and such other category of companies as prescribed by the rules to constitute a Nomination and Remuneration Committee. Unlike in the earlier companies act where the scope of remuneration committee was restricted to Directors appointed under Schedule XIII, the new Act extends its scope to senior management and overall remuneration policy followed by a Company.
- The requirement of Stakeholders Relationship Committee arises in companies with more than 1000 shareholders/debenture holders/ security holders.

- Appointment of Director elected by small shareholders:- Section 151 of the Companies Act 2013 provides for appointment of director elected by all listed companies. However it is not made mandatory.
- Prohibition on forward dealing in securities of company by Director or key managerial personnel and Prohibition on Insider Trading of Securities:- Section 194 and 195 of the Companies Act 2013 consists of provisions related to prohibition of Insider Trading. Being a part of the companies act this provisions cover all companies.
- Appointment of key managerial personnel in prescribed companies will bring more accountability to persons who holds key positions in a company
- Secretarial Audit:- The provisions regarding secretarial audit provided under Section 204 not only help the companies to avoid non-compliance with applicable legal provisions due to lack of awareness or knowledge but also act as deterrent on willful non-compliance of applicable legal provisions.
- Class action:- Section 245 of the Act provides for class action which enable shareholders/depositors to approach the tribunal when the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interest of the company or its members or depositors. It provides for claiming damages from the company, its directors or the auditors or any expert or advisor who has given any incorrect or misleading statement to the company.
- Voting through electronic means:- Voting through electronic means provided under Section 108 will enable wider participation of shareholders in passing resolutions in respect of various items to be transacted in general meetings.
- Corporate social responsibility: Section 135 deals with Corporate Social Responsibility wherein it is made mandatory for all profit making companies to spent a fixed percentage (2%) of the average net profit in the preceding 3 financial years towards corporate social responsibility where the eligible heads of expenditure is prescribed in Schedule VII. A company has to constitute a Board level committee to monitor Corporate Social Responsibility activities.
- Internal Audit:- Section 138 of the Act mandates appointment of Internal Auditor by prescribed class of companies. Internal Audit being an important aspect in the overall monitoring of the functions of a Company, bringing it in the Companies Act itself is step in the right direction as it gives more importance and wider implementation of internal audit.

Apart from the legal provisions mentioned above, the new companies act also define certain important terms which are relevant from the governance point of view but not find a place in the erstwhile companies act 1956. The following are important definitions incorporated in the Companies Act 2013:-

- Chief Executive Officer
- Chief Financial Officer
- Independent Director

- Key Managerial Personnel
- Officer
- Promoter
- Related Party

## **FINDINGS**

From the above it can be seen that the Companies Act 2013 has incorporated a number of provision with view to implement and improve the corporate governance framework in the Indian companies. It is also important to note that the applicability of these provisions are made on a selective manner to ensure that companies which meets certain thresholds are only subjected to these requirements.

## **CONCLUSIONS**

In India only listed companies are subjected to corporate governance requirements. However considering that a large number of unlisted companies whose healthy performance and orderly management is essential for the overall well being of country's business ecosystem there was need for a proper legal framework. The Companies Act 2013 has incorporated adequate provisions to address this situation. The analysis of the provisions shows that they have been made applicable to those companies which the government feels are important based certain parameters. As a result of these we can expect a major change in the way the unlisted companies are operated in India and also considerable increase in the governance standards especially from the transparency and accountability perspective.

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