India's Policy Transformation in Corporate Governance

Why in News?

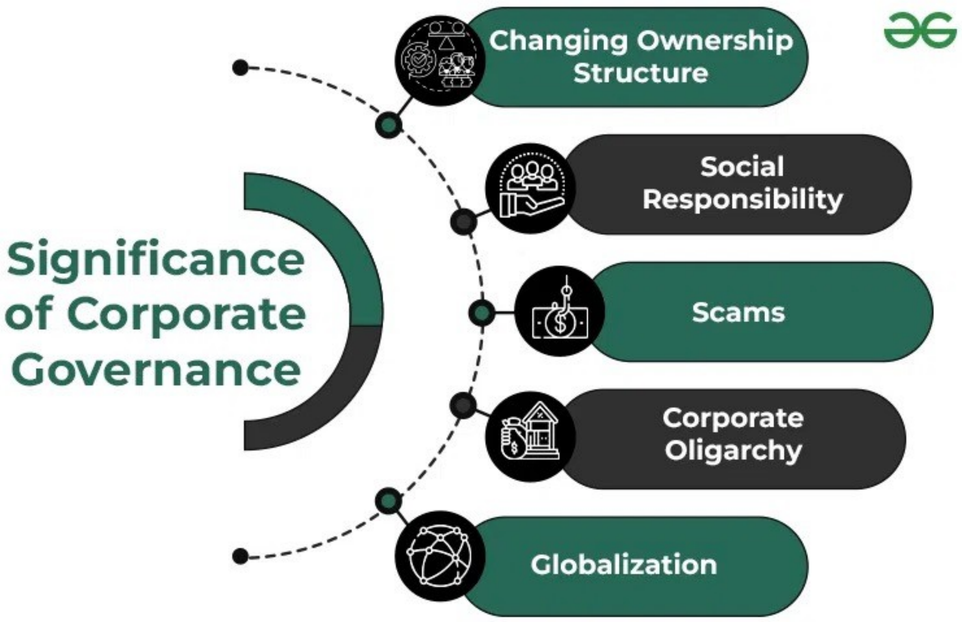
India's economic trajectory was defined by two key policy shifts: the planned development of 1951 and the liberalization of 1991, both catalyzing growth through distinct government roles.

What is corporate governance?

- **Corporate**- A business organisation having a separate legal entity, ie an identity distinct from its owners, is called a corporation or a company in India.
- ***Section 2(11) of the Companies Act***, 2013 defines "body corporate" or "corporation" to include
    - Private companies
    - Public companies
    - Personal companies
    - Small companies
    - Limited Liability Partnerships (LLPs)
    - Foreign companies
    - Companies incorporated outside India
- **Corporate governance** - It refers to the system of rules, practices, and processes by which a company is directed and controlled.
- It involves balancing the interests of a company's many stakeholders, such as shareholders, management, customers, suppliers, financiers, government, and the community.
- **Importance** - It ensures accountability, fairness, and transparency in a company's relationship with its stakeholders.

How corporates are governed in India?

- **Legislations**
  - **Companies Act, 2013 -** It is the primary legislation governing corporate governance in India.
  - It includes provisions related to the composition & functions of the board, appointing auditor, disclosures, & shareholder rights.
  - **Securities Contracts (Regulation) Act, 1956**- It governs the listing of securities and enforces regulations for stock exchanges and listed companies, contributing to corporate governance.
- **Regulations** - *SEBI (Listing Obligations and Disclosure Requirements) Regulations*, 2015 apply to listed companies.
- It mandate specific corporate governance norms, including board composition, audit committees, and the role of independent directors.
- **Guidelines -** *National Guidelines on Responsible Business Conduct (NGRBC)* was issued by the Ministry of Corporate Affairs.
- It encourage businesses to adopt sustainable and ethical practices.



What are the major episodes of policy transformations in India?

- **First major transformation** - The launch of the *First Five-Year Plan* in 1951 marked the beginning of India's planned economic development.
- The *emphasis on public-sector development*, particularly in heavy industries, with significant private investment was also taking place.
- Despite *modest growth*, it marked a substantial shift from the pre-Independence annual growth rate of 0.5%, achieving a *nine-fold increase*.
- **Low growth episode**– It was marked by *droughts, a new agricultural policy, and political instability*, this period saw relatively low economic growth.
- **Second major transformation** - The 1980s saw the *beginning of higher growth*, but a significant policy shift from public to private sector investment occurred after the *1991 liberalisation.*

- The most profound change post-1991 was the financial liberalisation, including opening banking and mutual funds to the private sector and reforming the share market.
- _New capital issues_ by non-government public limited companies grew significantly, from Rs.600 crore in 1981-82 to Rs.1.5 trillion in 2021-22.
- **Evolution of India's trade patterns**- India's share in world merchandise exports declined from 1.9% in 1951 to 0.4% by 1980 but has since recovered to 1.8%.
- India's share in global trade in commercial services increased from 0.6% in 1990 to 4.3% in 2023.

1951-1965	• First major transformation
Mid-1960s to Late-1970s	• Low growth episode
Post-1980 & Liberalisation in 1991	• Second major transformation

What are the challenges associated with corporate governance?

- **Conflict of interest-** Directors and management may face conflicts between their personal interests and those of the company, leading to unethical decisions.
- **Lack of independence-** Independent directors may not be truly independent, compromising their ability to provide unbiased oversight.
- **Ineffective board functioning-** Boards may be dominated by a few individuals, reducing their effectiveness in oversight and decision-making.
- **Weak enforcement of regulations-** Although laws are in place, the enforcement of corporate governance regulations can be inconsistent, allowing malpractices to persist.
- **Transparency issues-** Companies may fail to provide adequate and accurate information to stakeholders, undermining trust and accountability.
- **Cultural and ethical deficiencies-** A lack of emphasis on ethical behavior and corporate responsibility can lead to governance failures.

Political acceptability comes more readily to a government visibly involved in supporting non-corporate private sector, reducing income inequalities and regional disparities, and addressing caste concerns

What lies ahead?

- Shift to a neutral, market-friendly relationship to avoid cronyism and ensure fair competition.
- Reform PLI Scheme to foster a more dynamic corporate environment.
- Encourage the shift from family-managed to professionally managed enterprises

through stronger competition.
- Raise the competence of the Competition Commission for enhancing private sector management dynamism.
- Regulate monopoly infrastructure to prevent private exploitation.
- Encourage companies to adopt and integrate ethical practices and corporate social responsibility into their business models.
- Utilize technology for better governance practices, such as digital voting platforms for shareholders and automated compliance monitoring systems.

References

1. Business Standard | Policy Transformations for Corporate governance
2. Investopedia | Corporate Governance