THE CHANGING PARADIGM OF CORPORATE GOVERNANCE IN INDIA

ACGA Listed Company Workshop

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Character, Competence & Commitment
Business Realities of Corporate India

- Concentrated Ownership Structures
  - Currently in the Nifty 50, 45 (92%) of the 49 companies have promoters, and 26 (53%) of the 49 companies have promoter holding over 50%

- The “Owner Mindset”
  - Effective 50% + 1 = Board Control = Control

- Concentration of Power
  - Majority Shareholder + Chairman + MD

- Multiple Hats: The ‘Owner – Manager - Fiduciary’

- Not really limited liability
  - Promoter guarantees are commonplace
  - Promoter liabilities

- Business dependence on Promoter
The Implications of Concentrated Ownership

• De-jure, De-facto and Shadow Control

• Principal Cost > Agency Cost

• Regulatory Focus to nudge towards the Custodian Model
  – Trustee/Fiduciary Mindset
  – Separation of ownership and management
  – Stakeholder Approach- Fiduciary duties of directors
  – Long Termism
Key SEBI Committee Recommendations

• A Wholesome Board
  – Minimum six directors + Half to be IDs + One woman ID
  – Separation of the role of chairperson and the CEO/MD
  – Independence “in spirit”
  – Lead ID
  – Disclosure of Skills Matrix
  – Knowledge updation and enhanced interaction of NEDs with senior management

• Commitment to Role
  – Enhanced number of board and committee meetings
  – Increased focus of board on strategy, succession planning, risk management, budget, board evaluation and ESG
  – Enhanced role of board committees
Key SEBI Committee Recommendations

• Information sharing with controlling promoters / significant shareholders
  – Business Realities vs. Legal Framework
  – Access to Inside Information – “Legitimate Purpose” Exception
  – From “Shadows” to “Sunlight”
  – Access to Information Agreement
  – Eligible Counter-parties + Minimum Principles + Mandatory Disclosures + Opt-in

• Related Party Transactions
  – Promoters and promoter group entities holding 20% or more: Related Parties
  – Shareholders’ approval - Brand usage/ royalty payments of more than 5% of the turnover
Key SEBI Committee Recommendations

- Audit and Auditor related aspects
  - Enhanced audit and auditor related disclosures
  - Clarity in SEBI’s powers to take action against auditors in case of gross negligence (in addition to fraud/connivance)
  - Strengthening the role of the ICAI + independent functioning of the QRB

- Guiding principles for governance of PSEs
  - Transparent mandate + Disclosure of objectives and obligations
  - Independence from administrative ministry
  - Consolidating government stake under holding entity structure

- Capacity building in SEBI
The Institution of Independent Directors

• Tick the Box vs. True Spirit of Independence

• Appointment Process
  – Criteria: Objective and Subjective Assessment of Independence
  – Who votes? Minority Interests vs. Shareholder Democracy

• Role of an ID
  – Business as Usual
  – Crisis Situation
  – Succession Planning

• Functioning
  – Fiduciary duty (stakeholder interests, minority protection, trade offs)
  – Reliance on management
  – Liabilities, risk and reward imbalance
  – Constructive and not disruptive presence
Role of Auditors as Gatekeepers

• Expectation Gap
  – Is the auditing professional living up to the expectations?

• Conflicts faced by Auditors
  – Non-audit services
  – Potential employment with the Company

• Auditing the Auditors
  – The monitoring and enforcement of audit profession needs to be revamped
  – Are SEBI Committee Recommendations far-reaching enough?
The Other Gatekeepers: Hits & Misses

- **Statutory Fiduciaries**
  - Company Secretary/ Compliance Officer
  - Auditor
- **Other Third Parties**
  - Credit Rating Agencies
  - Proxy Advisory Firms
  - Analysts
  - Business Journalists
  - Whistle Blowers
- **Regulators (SEBI/ Stock Exchanges)**
- **Promoters/ Large Shareholders**
THANK YOU