

Chapter - Corporate Governance Initiatives

Government of India adopted the policy of liberalisation, privatization and globalisation (LPG) in India. Since then several policy initiatives have been taken to boost economic growth, efficiency and global competitiveness of Indian companies. Both legislative and non-legislative reforms have been carried out to improve governance in the corporate sector.

Need for Corporate Governance Reforms

The need for corporate governance has arisen because of the increasing concern about the non-compliance of standards of financial reporting and accountability by boards of directors and management of corporate inflicting heavy losses on investors.

The collapse of international giants like Enron, World Com of the US and Xerox of Japan are said to be due to the absence of good corporate governance and corrupt practices adopted by management of these companies and their financial consulting firms.

The failures of these multinational giants bring out the importance of good corporate governance structure making clear the distinction of power between the Board of Directors and the management which can lead to appropriate governance processes and procedures under which management is free to manage and board of directors is free to monitor and give policy directions.

In India, SEBI realised the need for good corporate governance and for this purpose appointed several committees such as Kumar Manglam Birla Committee, Naresh Chandra Committee and Narayana Murthy Committee.

Importance of Corporate Governance:

A good system of corporate governance is important on account of the following:

1. Investors and shareholders of a corporate company need protection for their investment due to lack of adequate standards of financial reporting and accountability. It has been noticed in India that companies raised capital from the

market at high valuation of their shares by projecting wrong picture of the company's performance and profitability.

2. Corporate governance is considered as an important means for paying heed to investors' grievances. Kumar Manglam Birla Committee on corporate governance found that companies were not paying adequate attention to the timely dissemination of required information to investors in by India. Though some measures have been taken by SEBI and RBI but much more required to be taken by the companies themselves to pay heed to the investors grievances and protection of their investment by adopting good standards of corporate governance.
3. The importance of good corporate governance lies in the fact that it will enable the corporate firms to (1) attract capital and (2) perform efficiently. This will help in winning investors confidence. Investors will be willing to invest in the companies with a good record of corporate governance.
4. Global Perspective. The extent to which corporate enterprises observe the basic principles of good corporate governance has now become an important factor for attracting foreign investment. In this age of globalisation when quantitative restrictions have been removed and trade barriers dismantled, the relationship between corporate governance and flows of foreign investment has become increasingly important.
5. Indispensable for healthy and vibrant stock market. An important advantage of strong corporate governance is that it is indispensable for a vibrant stock market. A healthy stock market is an important instrument for investors protection. A bane of stock market is insider trading. Insider trading means trading of shares of a company by insiders such directors, managers and other employees of the company on the basis of information which is not known to outsiders of the company.

Corporate Governance Initiatives in India

Corporate governance reforms in India involved a range of other initiatives including improvement in functioning of capital markets, effective minority shareholder protection, greater transparency & high standards of information disclosure, reforming board structures and streamlining board processes.

The government of India initiated the reforms in the governance process via government legislations and institutions in mid nineties. Several amendments were incorporated in the Companies Act 1956 to suit the needs of good corporate governance practice and statutory regulations were framed by the Securities and Exchange Board of India (SEBI). The Companies Bill 1997, The Companies (Amendment) Act, 1999, The Companies (Amendment) Act, 2000 and The Companies (Amendment) Act, 2001 were introduced with appropriate changes to make the Act more suitable with the time. Industry chambers, business associations and professional bodies also took voluntary initiatives to further the reform process.

SEBI initiated a large proportion of reforms to ensure better governance and development of efficient capital markets. Specific initiatives by SEBI included introduction norms for issuers, automation of stock exchanges, entry point criteria for public offers, modernization of market micro-structures and reformed regulations for mergers and takeovers. Numerous legislations were enacted from year 1992 to 2000 in this connection. Implementation of the recommendations of the K M Birla Committee report on corporate governance and SEBI regulations such as Substantial Acquisition of Shares and Takeovers 1997, Takeover Regulation 1997, Buy Back of Securities 1998, Employee Stock Option Scheme and Employee Stock Purchase Scheme Guidelines 1999 have far reaching consequences on corporate governance in India.

In late 1990s and early 2000 different governance codes were formulated by three distinct entities – The Confederation of Indian Industry (CII), The Department of Company Affairs (DCA) and The Securities and Exchange Board of India (SEBI). There was a broad consistency and consensus among the three in their recommendations for better governance.

The CII published the document named “The Desirable Code of Corporate Governance” in 1998 which outlines several policies that can be adopted by Indian firms in line with international corporate governance best practices.

The K M Birla Committee on Corporate Governance was set up by SEBI in May 1999 to suggest measures to improve corporate governance in India and draft a code of best practices with both mandatory and voluntary clauses.

The DCA of the Government of India brought several legislative amendments to The Companies Act 1956. It also set up a study group in May 2000 with the objective of further operationalizing the concept of corporate governance in India.

SEBI formed another committee named N.R. Narayana Murthy Committee in 2002 that consisted of experts from the chamber of commerce, stock exchanges, professionals and investors association. The Naryana Murthy committee suggested mandatory clauses such as reinforcing the responsibilities of audit committee, management of risks, raising standards of financial disclosures, defining the status of nominee directors and disclosure of non-executive directors' remuneration to shareholders among other recommendations.

The Government of India through DCA set up two committees – Naresh Chandra Committee and J J Irani Committee to strengthen corporate governance in India. The Naresh Chandra Committee was set up in August 2002 with the aim of examining various issues related to corporate governance.

The J. J. Irani Committee was formed in December 2004, by the Ministry of Corporate Affairs, Government of India with the responsibility to make recommendations on protection of the stakeholders and investors, reducing the size of Company Law and to deal with the parts related to the amendment of the Companies Act, 1956. The committee was also expected to examine the different perception on the concept paper received from the stakeholders.

In 2009, Ministry of Corporate Affairs (MCA) introduced Corporate Governance Voluntary Guidelines to improve corporate governance practices in Indian listed companies. The guidelines issued a series of recommendations based upon the mandatory and non-mandatory provision of Clause 49 of the Listing Agreement.

KUMAR MANGALAM BIRLA COMMITTEE(2000)

In early 1999, Securities and Exchange Board of India (SEBI) had set up a committee under Shri Kumar Mangalam Birla, member SEBI Board, to promote and raise the standards of good corporate governance. The report submitted by the committee is the first formal and comprehensive attempt to evolve a 'Code of Corporate Governance', in the context of prevailing conditions of governance in Indian companies, as well as the state of capital markets.

The Committee's terms of the reference were to:

1. suggest suitable amendments to the listing agreement executed by the stock exchanges with the companies and any other measures to improve the

standards of corporate governance in the listed companies, in areas such as continuous disclosure of material information, both financial and non-financial, manner and frequency of such disclosures, responsibilities of independent and outside directors;

2. draft a code of corporate best practices; and
3. suggest safeguards to be instituted within the companies to deal with insider information and insider trading.

The primary objective of the committee was to view corporate governance from the perspective of the investors and shareholders and to prepare a 'Code' to suit the Indian corporate environment. The committee had identified the Shareholders, the Board of Directors and the Management as the three key constituents of corporate governance and attempted to identify in respect of each of these constituents, their roles and responsibilities as also their rights in the context of good corporate governance.

Corporate governance has several claimants—shareholders and other stakeholders -which include suppliers, customers, creditors, and the bankers, the employees of the company, the government and the society at large. The Report had been prepared by the committee, keeping in view primarily the interests of a particular class of stakeholders, namely, the shareholders, who together with the investors form the principal constituency of SEBI while not ignoring the needs of other stakeholders.

Mandatory and non-mandatory recommendations

The committee divided the recommendations into two categories, namely, mandatory and non-mandatory. The recommendations which are absolutely essential for corporate governance can be defined with precision and which can be enforced through the amendment of the listing agreement could be classified as mandatory. Others, which are either desirable or which may require change of laws, may, for the time being, be classified as non-mandatory.

A. Mandatory Recommendations:

1. Applies To Listed Companies With Paid Up Capital Of Rs. 3 Crore And Above

2. Composition Of Board Of Directors –Optimum Combination Of Executive & Non-Executive Directors
3. Audit Committee –With 3 Independent Directors With One Having Financial And Accounting Knowledge.
4. Remuneration Committee
5. Board Procedures –At least 4 Meetings of the Board in a Year with Maximum Gap of 4 Months between 2 Meetings. To Review Operational Plans, Capital Budgets, Quarterly Results, Minutes Of Committee's Meeting. Director Shall Not Be A Member Of More Than 10 Committee And Shall Not Act As Chairman Of More Than 5 Committees Across All Companies
6. Management Discussion And Analysis Report Covering Industry Structure, Opportunities, Threats, Risks, Outlook, Internal Control System
7. Information Sharing With Shareholders

B. Non-Mandatory Recommendations:

1. Role Of Chairman
2. Remuneration Committee Of Board
3. Shareholders' Right For Receiving Half Yearly Financial Performance Postal Ballot Covering Critical Matters Like Alteration In Memorandum Etc
4. Sale Of Whole Or Substantial Part Of The Undertaking
5. Corporate Restructuring
6. Further Issue Of Capital
7. Venturing Into New Businesses

Clause 49 Of Listing Agreement

The company agrees to comply with the following provisions:

I. Board of Directors

(A) Composition of Board

- (i) The Board of directors of the company shall have an optimum combination of executive and non-executive directors with not less than fifty percent of the board of directors comprising of non-executive directors.
- (ii) Where the Chairman of the Board is a non-executive director, at least one-third of the Board should comprise of independent directors and in case he is an executive director, at least half of the Board should comprise of independent directors.
- (iii) For the purpose of the sub-clause (ii), the expression ‘independent director’ shall mean a non-executive director of the company who:
 - a. apart from receiving director’s remuneration, does not have any material pecuniary relationships or transactions with the company, its promoters, its directors, its senior management or its holding company, its subsidiaries and associates which may affect independence of the director;
 - b. is not related to promoters or persons occupying management positions at the board level or at one level below the board;
 - c. has not been an executive of the company in the immediately preceding three financial years;
 - d. is not a partner or an executive or was not partner or an executive during the preceding three years, of any of the following:
 - i) the statutory audit firm or the internal audit firm that is associated with the company, and
 - ii) the legal firm(s) and consulting firm(s) that have a material association with the company.
 - e. is not a material supplier, service provider or customer or a lessor or lessee of the company, which may affect independence of the director; and
 - f. is not a substantial shareholder of the company i.e. owning two percent or more of the block of voting shares.

Explanation

For the purposes of the sub-clause (iii):

- a. Associate shall mean a company which is an “associate” as defined in Accounting Standard (AS) 23, “Accounting for Investments in Associates in Consolidated Financial Statements”, issued by the Institute of Chartered Accountants of India.
 - b. “Senior management” shall mean personnel of the company who are members of its core management team excluding Board of Directors. Normally, this would comprise all members of management one level below the executive directors, including all functional heads.
 - c. “Relative” shall mean “relative” as defined in section 2(41) and section 6 read with Schedule IA of the Companies Act, 1956..
- (iv) Nominee directors appointed by an institution which has invested in or lent to the company shall be deemed to be independent directors.

Explanation:

“Institution’ for this purpose means a public financial institution as defined in Section 4A of the Companies Act, 1956 or a “corresponding new bank” as defined in section 2(d) of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 or the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 [both Acts].”

(B)Non executive directors’ compensation and disclosures

All fees/compensation, if any paid to non-executive directors, including independent directors, shall be fixed by the Board of Directors and shall require previous approval of shareholders in general meeting. The shareholders’ resolution shall specify the limits for the maximum number of stock options that can be granted to non-executive directors, including independent directors, in any financial year and in aggregate.

(C)Other provisions as to Board and Committees

- (i) The board shall meet at least four times a year, with a maximum time gap of three months between any two meetings. The minimum information to be made available to the board is given in **Annexure– I A**.
- (ii) A director shall not be a member in more than 10 committees or act as Chairman of more than five committees across all companies in which he is a director. Furthermore it should be a mandatory annual requirement for every director to inform the company about the committee positions he occupies in other companies and notify changes as and when they take place.

Explanation:

1. For the purpose of considering the limit of the committees on which a director can serve, all public limited companies, whether listed or not, shall be included and all other companies including private limited companies, foreign companies and companies under Section 25 of the Companies Act shall be excluded.
2. For the purpose of reckoning the limit under this sub-clause,

Chairmanship/ membership of the Audit Committee and the Shareholders' Grievance Committee alone shall be considered.

- (iii) The Board shall periodically review compliance reports of all laws applicable to the company, prepared by the company as well as steps taken by the company to rectify instances of non-compliances.

(D) Code of Conduct

- a. The Board shall lay down a code of conduct for all Board members and senior management of the company. The code of conduct shall be posted on the website of the company.
- b. All Board members and senior management personnel shall affirm compliance with the code on an annual basis. The Annual Report of the company shall contain a declaration to this effect signed by the CEO.

Explanation: For this purpose, the term “senior management” shall mean personnel of the company who are members of its core management team excluding Board of Directors.. Normally, this would comprise all members of management one level below the executive directors, including all functional heads.

II Audit Committee

(A) Qualified and Independent Audit Committee

A qualified and independent audit committee shall be set up, giving the terms of reference subject to the following:

- (i) The audit committee shall have minimum three directors as members. Two-thirds of the members of audit committee shall be independent directors.
- (ii) All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise.

Explanation 1: The term “financially literate” means the ability to read and understand basic financial statements i.e. balance sheet, profit and loss

account, and statement of cash flows.

Explanation 2: A member will be considered to have accounting or related financial management expertise if he or she possesses experience in finance or accounting, or requisite professional certification in accounting, or any other comparable experience or background which results in the individual's financial sophistication, including being or having been a chief executive officer, chief financial officer or other senior officer with financial oversight responsibilities.

- (iii) The Chairman of the Audit Committee shall be an independent director;
- (iv) The Chairman of the Audit Committee shall be present at Annual General Meeting to answer shareholder queries;
- (v) The audit committee may invite such of the executives, as it considers appropriate (and particularly the head of the finance function) to be present at the meetings of the committee, but on occasions it may also meet without the presence of any executives of the company. The finance director, head of internal audit and a representative of the statutory auditor may be present as invitees for the meetings of the audit committee;
- (vi) The Company Secretary shall act as the secretary to the committee.

(B) Meeting of Audit Committee

The audit committee should meet at least four times in a year and not more than four months shall elapse between two meetings. The quorum shall be either two members or one third of the members of the audit committee whichever is greater, but there should be a minimum of two independent members present.

(C) Powers of Audit Committee

The audit committee shall have powers, which should include the following:

1. To investigate any activity within its terms of reference.
2. To seek information from any employee.
3. To obtain outside legal or other professional advice.
4. To secure attendance of outsiders with relevant expertise, if it considers necessary.

(D) Role of Audit Committee

The role of the audit committee shall include the following:

1. Oversight of the company's financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct, sufficient and credible.
2. Recommending to the Board, the appointment, re-appointment and, if required, the replacement or removal of the statutory auditor and the fixation of audit fees.
3. Approval of payment to statutory auditors for any other services rendered by the statutory auditors.
4. Reviewing, with the management, the annual financial statements before submission to the board for approval, with particular reference to:
 - a. Matters required to be included in the Director's Responsibility Statement to be included in the Board's report in terms of clause (2AA) of section 217 of the Companies Act, 1956
 - b. Changes, if any, in accounting policies and practices and reasons for the same
 - c. Major accounting entries involving estimates based on the exercise of judgment by management
 - d. Significant adjustments made in the financial statements arising out of audit findings
 - e. Compliance with listing and other legal requirements relating to financial statements
 - f. Disclosure of any related party transactions
 - g. Qualifications in the draft audit report.
5. Reviewing, with the management, the quarterly financial statements before submission to the board for approval
6. Reviewing, with the management, performance of statutory and internal auditors, adequacy of the internal control systems.
7. Reviewing the adequacy of internal audit function, if any, including the structure of the internal audit department, staffing and seniority of the official heading the department, reporting structure coverage and frequency of internal audit.
8. Discussion with internal auditors any significant findings and follow up there on.
9. Reviewing the findings of any internal investigations by the internal auditors into matters where there is suspected fraud or irregularity or a failure of internal control systems of a material nature and reporting the

matter to the board.

10. Discussion with statutory auditors before the audit commences, about the nature and scope of audit as well as post-audit discussion to ascertain any area of concern.
11. To look into the reasons for substantial defaults in the payment to the depositors, debenture holders, shareholders (in case of non payment of declared dividends) and creditors.
12. To review the functioning of the Whistle Blower mechanism, in case the same is existing.
13. Carrying out any other function as is mentioned in the terms of reference of the Audit Committee.

Explanation (i): The term "related party transactions" shall have the same meaning as contained in the Accounting Standard 18, Related Party Transactions, issued by The Institute of Chartered Accountants of India.

Explanation (ii): If the company has set up an audit committee pursuant to provision of the Companies Act, the said audit committee shall have such additional functions / features as is contained in this clause.

(E) Review of information by Audit Committee

The Audit Committee shall mandatorily review the following information:

1. Management discussion and analysis of financial condition and results of operations;
2. Statement of significant related party transactions (as defined by the audit committee), submitted by management;
3. Management letters / letters of internal control weaknesses issued by the statutory auditors;
4. Internal audit reports relating to internal control weaknesses; and
5. The appointment, removal and terms of remuneration of the Chief internal auditor shall be subject to review by the Audit Committee

III. Subsidiary Companies

- i. At least one independent director on the Board of Directors of the holding company shall be a director on the Board of Directors of a material non listed Indian subsidiary company.
- ii. The Audit Committee of the listed holding company shall also review

the financial statements, in particular, the investments made by the unlisted subsidiary company.

- iii. The minutes of the Board meetings of the unlisted subsidiary company shall be placed at the Board meeting of the listed holding company. The management should periodically bring to the attention of the Board of Directors of the listed holding company, a statement of all significant transactions and arrangements entered into by the unlisted subsidiary company.

Explanation 1: The term “material non-listed Indian subsidiary” shall mean an unlisted subsidiary, incorporated in India, whose turnover or net worth (i.e. paid up capital and free reserves) exceeds 20% of the consolidated turnover or net worth respectively, of the listed holding company and its subsidiaries in the immediately preceding accounting year.

Explanation 2: The term “significant transaction or arrangement” shall mean any individual transaction or arrangement that exceeds or is likely to exceed 10% of the total revenues or total expenses or total assets or total liabilities, as the case may be, of the material unlisted subsidiary for the immediately preceding accounting year.

Explanation 3: Where a listed holding company has a listed subsidiary which is itself a holding company, the above provisions shall apply to the listed subsidiary insofar as its subsidiaries are concerned.

IV. Disclosures

(A)Basis of related party transactions

- (i) A statement in summary form of transactions with related parties in the ordinary course of business shall be placed periodically before the audit committee.
- (ii) Details of material individual transactions with related parties which are not in the normal course of business shall be placed before the audit committee.
- (iii) Details of material individual transactions with related parties or others, which are not on an arm’s length basis should be placed before the audit committee, together with Management’s justification for the

same..

(B)Disclosure of Accounting Treatment

Where in the preparation of financial statements, a treatment different from that prescribed in an Accounting Standard has been followed, the fact shall be disclosed in the financial statements, together with the management's explanation as to why it believes such alternative treatment is more representative of the true and fair view of the underlying business transaction in the Corporate Governance Report.

(C) Board Disclosures – Risk management

The company shall lay down procedures to inform Board members about the risk assessment and minimization procedures. These procedures shall be periodically reviewed to ensure that executive management controls risk through means of a properly defined framework.

(D)Proceeds from public issues, rights issues, preferential issues etc.

When money is raised through an issue (public issues, rights issues, preferential issues etc.), it shall disclose to the Audit Committee, the uses / applications of funds by major category (capital expenditure, sales and marketing, working capital, etc), on a quarterly basis as a part of their quarterly declaration of financial results. Further, on an annual basis, the company shall prepare a statement of funds utilized for purposes other than

those stated in the offer document/prospectus/notice and place it before the audit committee. Such disclosure shall be made only till such time that the full money raised through the issue has been fully spent. This statement shall be certified by the statutory auditors of the company. The audit committee shall make appropriate recommendations to the Board to take up steps in this matter.

(E)Remuneration of Directors

- (i) All pecuniary relationship or transactions of the non-executive directors vis-à-vis the company shall be disclosed in the Annual Report.
- (ii) Further the following disclosures on the remuneration of directors shall

be made in the section on the corporate governance of the Annual Report:

- (a) All elements of remuneration package of individual directors summarized under major groups, such as salary, benefits, bonuses, stock options, pension etc.
 - (b) Details of fixed component and performance linked incentives, along with the performance criteria.
 - (c) Service contracts, notice period, severance fees.
 - (d) Stock option details, if any – and whether issued at a discount as well as the period over which accrued and over which exercisable.
- (iii) The company shall publish its criteria of making payments to non-executive directors in its annual report. Alternatively, this may be put up on the company's website and reference drawn thereto in the annual report.
- (iv) The company shall disclose the number of shares and convertible instruments held by non-executive directors in the annual report.
- (v) Non-executive directors shall be required to disclose their shareholding (both own or held by / for other persons on a beneficial basis) in the listed company in which they are proposed to be appointed as directors, prior to their appointment. These details should be disclosed in the notice to the general meeting called for appointment of such director

(F) Management

- (i) As part of the directors' report or as an addition thereto, a Management Discussion and Analysis report should form part of the Annual Report to the shareholders. This Management Discussion & Analysis should include discussion on the following matters within the limits set by the company's competitive position:
- i. Industry structure and developments.
 - ii. Opportunities and Threats.
 - iii. Segment-wise or product-wise performance.
 - iv. Outlook
 - v. Risks and concerns.
 - vi. Internal control systems and their adequacy.

vii. Discussion on financial performance with respect to operational performance.

viii. Material developments in Human Resources / Industrial Relations front, including number of people employed.

- (ii) Senior management shall make disclosures to the board relating to all material financial and commercial transactions, where they have personal interest, that may have a potential conflict with the interest of the company at large (for e.g. dealing in company shares, commercial dealings with bodies, which have shareholding of management and their relatives etc.)

Explanation: For this purpose, the term "senior management" shall mean personnel of the company who are members of its core management team excluding the Board of Directors). This would also include all members of management one level below the executive directors including all functional heads.

(G) Shareholders

- (i) In case of the appointment of a new director or re-appointment of a director the shareholders must be provided with the following information:
- (a) A brief resume of the director;
 - (b) Nature of his expertise in specific functional areas;
 - (c) Names of companies in which the person also holds the directorship and the membership of Committees of the Board; and
 - (d) Shareholding of non-executive directors as stated in Clause 49 (IV) (E) (v) above
- (ii) Quarterly results and presentations made by the company to analysts shall be put on company's web-site, or shall be sent in such a form so as to enable the stock exchange on which the company is listed to put it on its own web-site.
- (iii) A board committee under the chairmanship of a non-executive director shall be formed to specifically look into the redressal of shareholder and investors complaints like transfer of shares, non-receipt of balance sheet, non-receipt of declared dividends etc. This Committee shall be

designated as 'Shareholders/Investors Grievance Committee'.

- (iv) To expedite the process of share transfers, the Board of the company shall delegate the power of share transfer to an officer or a committee or to the registrar and share transfer agents. The delegated authority shall attend to share transfer formalities at least once in a fortnight.

V.CEO/CFO certification

The CEO, i.e. the Managing Director or Manager appointed in terms of the Companies Act, 1956 and the CFO i.e. the whole-time Finance Director or any other person heading the finance function discharging that function shall certify to the Board that:

- (a) They have reviewed financial statements and the cash flow statement for the year and that to the best of their knowledge and belief :
 - (i) these statements do not contain any materially untrue statement or omit any material fact or contain statements that might be misleading;
 - (ii) these statements together present a true and fair view of the company's affairs and are in compliance with existing accounting standards, applicable laws and regulations.
- (b) There are, to the best of their knowledge and belief, no transactions entered into by the company during the year which are fraudulent, illegal or violative of the company's code of conduct.
- (c) They accept responsibility for establishing and maintaining internal controls and that they have evaluated the effectiveness of the internal control systems of the company and they have disclosed to the auditors and the Audit Committee, deficiencies in the design or operation of internal controls, if any, of which they are aware and the steps they have taken or propose to take to rectify these deficiencies.
- (d) They have indicated to the auditors and the Audit committee
 - (i) significant changes in internal control during the year;
 - (ii) significant changes in accounting policies during the year and that the same have been disclosed in the notes to the financial statements; and
 - (iii) instances of significant fraud of which they have become aware and the involvement therein, if any, of the management or an employee having a significant role in the company's internal control system

VI. Report on Corporate Governance

- (i) There shall be a separate section on Corporate Governance in the Annual Reports of company, with a detailed compliance report on Corporate Governance. Non-compliance of any mandatory requirement of this clause with reasons thereof and the extent to which the non-mandatory requirements have been adopted should be specifically highlighted. The suggested list of items to be included in this report is given in **Annexure- I C** and list of non-mandatory requirements is given in **Annexure – I D**.
- (ii) The companies shall submit a quarterly compliance report to the stock exchanges within 15 days from the close of quarter as per the format given in **Annexure I B**. The report shall be signed either by the Compliance Officer or the Chief Executive Officer of the company

VII. Compliance

- (1) The company shall obtain a certificate from either the auditors or practicing company secretaries regarding compliance of conditions of corporate governance as stipulated in this clause and annex the certificate with the directors' report, which is sent annually to all the shareholders of the company. The same certificate shall also be sent to the Stock Exchanges along with the annual report filed by the company.
- (2) The non-mandatory requirements given in **Annexure – I D** may be implemented as per the discretion of the company. However, the disclosures of the compliance with mandatory requirements and adoption (and compliance) / non-adoption of the non-mandatory requirements shall be made in the section on corporate governance of the Annual Report.

➤ Class Action:

The concept of Class Action Suits is among one of the many novelties introduced by the Companies Act, 2013. Though the concept per se is not new but in Indian context it has found statutory recognition and enforceability now only by means of Companies Act 2013.

The first time class action suit came to the spotlight in the context of securities market was when the Satyam scam broke out in 2009. At that time, the Indian investors in India couldn't take any legal recourse against the company while their counterparts in USA filed class action suit claiming damages from the company and the auditing firm. Credit to the Satyam scam, India has introduced

class action suit in the new Companies Act, 2013 by means of Section 245 which is yet to be notified by the Ministry of Corporate Affairs.

In simple terms, a class action suit refers to a lawsuit that allows a large number of people with a common interest in a matter to sue or be sued as a group. It is a procedural device enabling one or more plaintiffs to file and prosecute a litigation on behalf of a larger group or class, wherein such class has common rights and grievances.

PROVISIONS RELATING TO CLASS ACTION SUIT AS CONTAINED IN COMPANIES ACT, 2013

Section 245 of the Companies Act, 2013 (Act) contains provisions regarding Class Action Suits which are discussed in detail below:

As per Section 245(1) read with Section 245(3), a Class Action Suit may be filed by:

1. Member or members or any class of them, as described below –
 - in the case of a company having a share capital,
 - i any 100 or more members of the company, or members equal to or exceeding 10% of the total number of its members, whichever is less, or
 - ü any member or members singly or jointly holding at least 10% of the issued share capital of the company,subject to the condition that the applicant or applicants has or have paid all calls and other sums due on his or their shares
 - in the case of a company not having a share capital, members equal to or exceeding 1/5th of the total number of its members.
2. Depositor or depositors or any class of them, as described below –
 - i any 100 or more depositors of the company, or depositors equal to or exceeding 10% of the total number of its depositors, whichever is less, or
 - ü any depositor or depositors singly or jointly holding at least 10% of the total value of outstanding deposits of the company.
3. The Central Government, if it is of the opinion that the affairs of the company are being conducted in a manner prejudicial to public interest

Before which authority class action suit needs to be filed?

Application for class action suit has to be filed before the National Company Law Board Tribunal (NCLT/Tribunal).

When can a Class Action Suit be filed?

Members or depositors or any class of them, as indicated above, may file a class action suit if they are of the opinion that the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interests of the company or its members or depositors seeking all or any of the following orders, namely:—.

- (a) to restrain the company from committing an act which is *ultra vires* the articles or memorandum of the company;
- (b) to restrain the company from committing breach of any provision of the company's memorandum or articles;
- (c) to declare a resolution altering the memorandum or articles of the company as void if the resolution was passed by suppression of material facts or obtained by mis-statement to the members or depositors;
- (d) to restrain the company and its directors from acting on such resolution;
- (e) to restrain the company from doing an act which is contrary to the provisions of this Act or any other law for the time being in force;
- (f) to restrain the company from taking action contrary to any resolution passed by the members;
- (g) to claim damages or compensation or demand any other suitable action from or against—
 - (i) the company or its directors for any fraudulent, unlawful or wrongful act or omission or conduct or any likely act or omission or conduct on its or their part;
 - (ii) the auditor including audit firm of the company for any improper or misleading statement of particulars made in his audit report or for any fraudulent, unlawful or wrongful act or conduct; or
 - (iii) any expert or advisor or consultant or any other person for any incorrect or misleading statement made to the company or for any

fraudulent, unlawful or wrongful act or conduct or any likely act or conduct on his part;

(h) to seek any other remedy as the Tribunal may deem fit.

Against whom a Class Action Suit can be filed?

Class action suit can be filed against the

- Company,
- Any of its directors
- Auditor, including audit firm
- Expert or advisor or consultant or any other person

In case of any claim against an audit firm, the liability shall be of the firm as well as of each partner who was involved in making any improper or misleading statement of particulars in the audit report or who acted in a fraudulent, unlawful or wrongful manner

Penalty for non-compliance of order passed by Tribunal

Any company which fails to comply with an order passed by the Tribunal under Section 245 shall be punishable with fine which shall not be less than Rs. 5 Lakhs but which may extend to Rs. 25 Lakhs and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 3 years and with fine which shall not be less than Rs. 25,000/- but which may extend to Rs. 1,00,000/-.

Under Section 425 of the Companies Act, 2013 the Tribunal has also been conferred the same jurisdiction, powers and authority in respect of contempt of its orders as conferred on High Court under the Contempt of Courts Act, 1971.

Other points relating to Class Action Suits

- The cost or expenses connected with the publication of the public notice shall be borne by the applicant and shall be defrayed by the company or any other person responsible for any oppressive act.
- Any order passed by the Tribunal shall be binding on the company and all its members, depositors and auditor including audit firm or expert or consultant or advisor or any other person associated with the company.
- Provisions relating to class action suits do not apply to a banking company.

Difference between application for prevention of oppression and mismanagement u/s 241 to 244 and Class Action Suits under Section 245

	Prevention of oppression and mismanagement u/s 241 to 244	Class Action Suits <u>Section 245</u>
Who can file application?	Members of the Company	Members as well as deposit holders of the company
Against whom application can be filed?	Company and its statutory appointees	Company, Any of its directors Auditor, including audit firm Expert or advisor or consultant or any other person
Matters for which application can be filed	Any current or past activity or to prevent recurrence	Any current, past or future activity, including to desist from one or more particular action that have not been taken yet.