SEBI and Corporate Governance

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Abstract

Corporate governance is a key element in improving the economic efficiency of a firm. Good corporate governance also helps ensure that corporations take into account the interests of a wide range of constituencies, as well as of the communities within which they operate. Furthermore, it ensures that their Boards are accountable to the shareholders. This, in turn, helps assure that corporations operate for the benefit of society as a whole. While large profits can be made taking advantage of the Asymmetry between stakeholders in the short run, balancing the interests of all stakeholders alone will ensure survival and growth in the long run. This includes, for instance, taking into account societal concerns about labor and the environment. Corporate governance initiatives in India began in 1998 with the desirable code of corporate governance – a voluntary code published by the CII, and the first formal regulatory framework for listed companies specifically for corporate governance, established by the SEBI. The latter was made in February 2000, following the recommendations of the Kumarmangalam Birla Committee Report.

The term “corporate governance” is susceptible to both broad and narrow definitions. In fact, many of the codes do not even attempt to articulate what is encompassed by the term. The motives for the several corporate governance postulates engaged in these definitions vary, depending on the participant concerned. The focal subjects also vary accordingly. The important point is that corporate governance is a concept, rather than an individual instrument. It includes debate on the appropriate Management and control structures of a company. Further it includes the rules relating to the power relations between owners, the Board of Directors, Management and, last but not least, the stakeholders such as employees, suppliers, customers and the public at large.

Key word: Corporate governance, Objective of corporate governance, SEBI, Objective of SEBI, meaning of corporate governance and SEBI

INTRODUCTION

A corporation is a congregation of various stakeholders, namely, customers, employees, investors, vendor partners, Government and society. A corporation should be fair and transparent to its stakeholders in all its transactions. This has become imperative in today's globalized business world where corporations need to access global pools of capital, need to attract and retain the best human capital from various parts of the world, need to partner with vendors on mega collaborations and need to live in harmony with the community. Unless a corporation embraces and demonstrates ethical conduct, it will not be able to succeed. Corporate governance is beyond the realm of law. It stems from the culture and mindset of management, and cannot be regulated by legislation alone. Corporate Governance deals with conducting the affairs of a company such that there is fairness to all stakeholders and that its actions benefit the greatest number of stakeholders. It is about openness, integrity and accountability. What legislation can and should do is to lay down a common framework – the “form” to ensure standards. The “substance” will ultimately determine the credibility and integrity of the process. Substance is inexorably linked to the mindset and ethical standards of management.
What is SEBI AND CORPORATE GOVERNANCE

Definition of SEBI: The regulatory body for the investment market in India. The purpose of this board is to maintain stable and efficient markets by creating and enforcing regulations in the marketplace. It was formed officially by the Government of India in 1992 with SEBI Act 1992 being passed by the Indian Parliament. SEBI is headquartered in the business district of Bandra Kurla Complex complex in Mumbai, and has Northern, Eastern, Southern and Western regional offices in New Delhi, Kolkata, Chennai and Ahmedabad. Controller of Capital Issues was the regulatory authority before SEBI came into existence; it derived authority from the Capital Issues (Control) Act, 1947. Initially SEBI was a non statutory body without any statutory power. However in 1995, the SEBI was given additional statutory power by the Government of India through an amendment to the Securities and Exchange Board of India Act 1992. In April, 1998 the SEBI was constituted as the regulator of capital markets in India under a resolution of the Government of India. The SEBI is managed by fix members, i.e. by the chairman who is nominated by central government & members, i.e. officers of central ministry, one member from the RBI & the remaining two are nominated by the central government. The office of SEBI is situated at Mumbai with its regional offices at Kolkata, Delhi & Chennai.

Definition of corporate governance: corporate governance is term that refers broadly to the rules, processes or laws by which business are operated, regulated and controlled the term can refer to internal factors defined by the officer, stockholders or constitution of a corporation, as well as to external forces such as consumer group, clients and government regulation. this report has been modulated by the SEBI through stock exchange via the listing agreement for the listed companies. Corporate governance seeks to report the effectiveness with which the management is discharging its responsibility of running the corporate affairs transparently. Corporate governance is the buzzword in financial circles today a number of reports and geodes on the subject have already been published internationally, notable among them are the report of the Cadbury committee.

SIGNIFICANCE SEBI AND CORPORATE GOVERNANCE

Often, increased attention on corporate governance is a result of financial crisis. For instance, the Asian financial crisis brought the subject of corporate governance to the surface in Asia. Further, recent scandals disturbed the otherwise placid and complacent corporate landscape in the US. These scandals, in a sense, proved to be serendipitous. They spawned a new set of initiatives in corporate governance in the US and triggered fresh debate in the European Union as well as in Asia. The many instances of corporate misdemeanors have also shifted the emphasis on compliance with substance, rather than form, and brought to sharper focus the need for intellectual honesty and integrity. This is because financial and non-financial disclosures made by any firm are only as good and honest as the people behind them. By this very principle, only those industrialists whose corporations are governed properly should be allowed to be a part of committees. This includes the Prime Minister and Finance Minister’s advisory councils, committees set up by the Confederation of Indian Industry (“CII”), the Securities and Exchange Board of India (“SEBI”), the Department of Company Affairs, ministries, and the boards of large banks and financial institutions. The majority of the definitions articulated in the codes relate corporate governance to “control” – of the company, of corporate management, or of company conduct or managerial conduct. Perhaps the simplest and most common definition of this sort is that provided by the Cadbury Report (U.K.), which is frequently quoted or paraphrased: “Corporate governance is the system by which businesses are directed and controlled.”

Good corporate governance should be integrated with company’s business strategy and objectives – good corporate governance includes transparency for corporate ions and inventors’, sound disclosure policies an communication. By proper execution of the bylaw of Corporate Governance the auditing process extends out of formalities, and establishing the internal controlling systems, especially auditing committee control leads to timely information disclosure and avoidance of intense fluctuations in
estimated benefits and price tampering. The role of all individuals in the company is as people's participation in determining their own destiny. Due to globalization of assets, the dimensions of corruption and fraud have been internationalized and the auditors are required to learn the new techniques of auditing to perform their new responsibilities in the emerging social accountability system. Undoubtedly, to fulfill the new role and responsibilities their mastery over auditing skills in risk-based auditing, analytical procedures, internal control and data-mining are among essentials as an auditor who is not expert in the abovementioned basis, fails to have the necessary skills to discover fraud and forgery in financial statements and cannot prevent misleading financial statements. The advantages of Corporate Governance bylaw is clarifying information, observing the rights of shareholders, establishing internal control systems, and reinforcing the relationship between the independent auditors and corporations. Since 1990s, the subject, "Corporate Governance", has been discussed by some industrial, developed countries like England, Australia and some European countries. The background of this concept goes back to a noted report, “Cadbury Report”, published in 1992. In this report the emphasis is given to establishing of internal control systems and internal auditing systems. Later on, disclosure of "Watergate Elections" in USA and the cheating in US assets market in 2001, led to approval of a law called "Sarbanes-Oxley", known as Corporate Governance. Since 2004, Corporate Governance law- OECD or "Sarbanes-Oxley"- has been enforced in Western Europe, England, Australia, Canada and US. Unfortunately no attempts have been made in the third world developing countries. Meanwhile, in Corporate Governance law, special emphasis is given to establishing an internal auditing system and internal auditing committee. Relationships between managers and independent auditors are formed via auditing committee sebi is also has been very proactive in the promotion of corporate governance among listed companies, it has so far appointed two committees (in 1999 and 2002) on the subject and made it obligatory for the listed companies to comply with a given set of corporate governance requirement through the mechanism of listing agreement.

OBJECTIVE OF CORPORATE GOVERNANCE:

The fundamental objective of corporate governance is investor protection and the enhancement of shareholders’ wealth, keeping in view the interests of other stakeholder’s corporate governance report seeks in report the effective with which the management is discharging its responsibility towards attaining this objective. In other word Corporate Governance is a set of relations among the shareholders, managers and auditors of a corporation which ensures controlling system in order to observe the rights of minor shareholders, proper execution of the enactments of the assembly, and to prevent possible misuses. This law which is based on responsiveness and social accountability includes a set of responsibilities to be handled by company managers to raise responsiveness and transparency. The subject of Corporate Governance is the relationship among managers, Board of Directors, shareholders and other stakeholders. Corporate Governance provides a structure by which corporate goals are defined, and the methods of gaining them and the performance control are specified. An ideal Corporate Governance should encourage the board of directors and the managers to pursue the goals beneficial to the corporate and shareholders and facilitate the effective control on the process.

OBJECTIVE OF SEBI:

The basic objectives of the Board were identified as:

- to protect the interests of investors in securities;
- to promote the development of Securities Market;
- to regulate the securities market and
- for matters connected therewith or incidental thereto.

Since its inception SEBI has been working targeting the securities and is attending to the fulfillment of its objectives with commendable zeal and dexterity. The improvements in the securities markets like capitalization requirements, margining, establishment of clearing corporations etc. reduced the risk of credit and also reduced the market.
SEBI has introduced the comprehensive regulatory measures, prescribed registration norms, the eligibility criteria, the code of obligations and the code of conduct for different intermediaries like, bankers to issue, merchant bankers, brokers and sub-brokers, registrars, portfolio managers, credit rating agencies, underwriters and others. It has framed bye-laws, risk identification and risk management systems for Clearing houses of stock exchanges, surveillance system etc. which has made dealing in securities both safe and transparent to the end investor. Another significant event is the approval of trading in stock indices (like S&P CNX Nifty & Sensex) in 2000. A market Index is a convenient and effective product because of the following reasons:

- It acts as a barometer for market behavior;
- It is used to benchmark portfolio performance;
- It is used in derivative instruments like index futures and index options;
- It can be used for passive fund management as in case of Index Funds.

Two broad approaches of SEBI is to integrate the securities market at the national level, and also to diversify the trading products, so that there is an increase in number of traders including banks, financial institutions, insurance companies, mutual funds, primary dealers etc. to transact through the Exchanges. In this context the introduction of derivatives trading through Indian Stock Exchanges permitted by SEBI in 2000 AD is a real landmark. SEBI appointed the L. C. Gupta Committee in 1998 to recommend the regulatory framework for derivatives trading and suggest bye-laws for Regulation and Control of Trading and Settlement of Derivatives Contracts. The Board of SEBI in its meeting held on May 11, 1998 accepted the recommendations of the committee and approved the phased introduction of derivatives trading in India beginning with Stock Index Futures. The Board also approved the "Suggestive Bye-laws" as recommended by the Dr LC Gupta Committee for Regulation and Control of Trading and Settlement of Derivatives Contracts.

SEBI then appointed the J. R. Verma Committee to recommend Risk Containment Measures (RCM) in the Indian Stock Index Futures Market. The report was submitted in November 1998. However the Securities Contracts (Regulation) Act, 1956 (SCRA) required amendment to include "derivatives" in the definition of securities to enable SEBI to introduce trading in derivatives. The necessary amendment was then carried out by the Government in 1999. The Securities Laws (Amendment) Bill, 1999 was introduced. In December 1999 the new framework was approved. Derivatives have been accorded the status of 'Securities'. The ban imposed on trading in derivatives in 1969 under a notification issued by the Central Government was revoked. Thereafter SEBI formulated the necessary regulations/bye-laws and intimated the Stock Exchanges in the year 2000. The derivative trading started in India at NSE in 2000 and BSE started trading in the year 2001.

THE KUMARMANGALAM BIRLA COMMITTEE ON CORPORATE GOVERNANCE

SEBI had constituted a Committee on May 7, 1999 under the chairmanship of Shri Kumarmangalam Birla, then Member of the SEBI Board “to promote and raise the standards of corporate governance”. Based on the recommendations of this Committee, a new clause 49 was incorporated in the Stock Exchange Listing Agreements (“Listing Agreements”). And also The recommendations of the Kumarmangalam Birla Committee on Corporate Governance (the “Recommendations”) are set out in Enclosure I to this report.

This was the first committee and its report the first report on corporate governance, which brought real focus and due attention to the subject. The report has been discussed an debated and is considered a milestone on the subject in our country. – The following extracts from the report of this committee outline the background of its setting: - corporate governance is considered an important instrument of investor protection and it is there for, apriority on SEBI agenda. to further improve the level of corporate governance, need was felt for a comprehensive approach at its stage of development of the capital market, to accelerate the adoption of globally acceptable practices of corporate governance.

CLAUS 49 : CORPORATE GOVERNANCE : the company agrees to comply with the following provisions : 1)Board of directors : a)composition of board :the board of directors of the company shall
have an optimum combination of executive and non-executive directors. b) non-executive directors compensation and disclosures: all fees/compensation, if any paid to non-executive directors, including indecent don’t directors, shall be fixed by the board of directors and shall require previous approval of shareholders in general meeting. c) other provisions as to board and committees: The board shall meet at least four times a year, with a maximum time gap of four months between any two meetings. d) Code of conduct: 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. 2) Audit committee: a) Qualified and independent audit committee: a qualified and independent audit committee shall be set have minimum three directors as members. two thirds of the members of audit committee shall be independent directors. – all members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise. B) meeting of audit committee: the audit committee should meet at least four times in a year and not more than for months shall elapse between two meetings. the quorum shall be either two members or one third of the members of the audit committee. C) powers of audit committee: The audit committee shall have powers, which include the following: C-1) The investigate any activity within its terms of reference C-2) To seek information from any employee C-3) To obtain outside legal or other professional advice C-4) To secure attendance of outsiders with relevant expertise. D) Role of audit committee: -over sight 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. E) review of information by audit committee: management discussion and analysis of financial condition and results of operation: 3) subsidiary companies: the minutes of the board meetings of the unlisted company shall be placed at the board meeting of the listed holding company. 4) disclosures: A. basis of related party transaction B. Disclosure of accounting treatment C. board disclosures (risk – management) – management. 5) Report on corporate governance: The shall be separate section an corporate governance in the annual report of company. 6) Compliance: the company shall obtain a certificate from either the auditors or practicing company secretaries.

FINANCIAL REPORTING AND DISCLOSURES

Financial disclosure is a critical component of effective corporate governance. SEBI set up an Accounting Standards Committee, as a Standing Committee, under the chairmanship of Shri Y. H. Malegam with the following objectives:

- To review the continuous disclosure requirements under the listing agreement for listed companies;
- To provide input to the Institute of Chartered Accountants of India (“ICAI”) for introducing new accounting standards in India; and
- To review existing Indian accounting standards, where required and to harmonies these accounting standards and financial disclosures on par with international practices.

SEBI has interacted with the ICAI on a continuous basis in the issuance of recent Indian accounting standards on areas including segment reporting, related party disclosures, consolidated financial statements, earnings per share, accounting for taxes on income, accounting for investments in associates in consolidated financial statements, discontinuing operations, interim financial reporting, intangible assets, financial reporting of interests in joint ventures and impairment of assets. With the introduction of these recent Indian accounting standards, financial reporting practices in India are almost on par with International Accounting Standards.

IMPLEMENTATION OF CORPORATE GOVERNANCE REQUIREMENTS

The Recommendations were implemented through Clause 49 of the Listing Agreements, in a phased manner by SEBI. They were made applicable to all companies in the BSE 200 and S&P C&X Nifty indices, and all newly listed companies, as of March 31, 2001. The applicability of the Recommendations was extended to companies with a paid up capital of Rs. 100 million or with a net
worth of Rs. 250 million at any time in the past five years, as of March 31, 2002. In respect of other listed companies with a paid up capital of over Rs. 30 million, the requirements were made applicable as of March 31, 2003. The accounting standards issued by the ICAI, which are applicable to all companies under sub-section 3A of Section 211 of the Companies Act, 1956, were specifically made applicable to all listed companies for the financial year ended March 31, 2002, under the Listing Agreements.

SUMMARY

Corporate governance is a key element in improving the economic efficiency of a firm. Good corporate governance also helps ensure that corporations take into account the interests of a wide range of constituencies, as well as of the communities within which they operate. Further, it ensures that their Boards are accountable to the shareholders. This, in turn, helps assure that corporations operate for the benefit of society as a whole. While large profits can be made taking advantage of the asymmetry between stakeholders in the short run, balancing the interests of all stakeholders alone will ensure survival and growth in the long run. It includes, for instance, taking into account societal concerns about labor and the environment. Corporate governance initiatives in India began in 1998 with the Desirable Code of Corporate Governance – a voluntary code published by the CII, and the first formal regulatory framework for listed companies specifically for corporate governance, established by the SEBI. The latter was made in February 2000, following the recommendations of the Kumarmangalam Birla Committee Report.

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