Inspira-Journal of Commerce, Economics & Computer Science (JCECS)
ISSN : 2395-7069 General Impact Factor : 2.0546, Volume 03, No. 04, Oct.-Dec., 2017, pp. 13-16

CORPORATE GOVERNANCE: STANDING OF INDIAN LISTED COMPANIES

Dr. (CA) Satyajit Dhar*
Dilip Kumar Pal**

ABSTRACT

The corporate governance compliance norms of Indian listed companies are mainly regulated by the Companies Act, 2013 and the SEBI (LODR) Regulations, 2015. To measure the corporate governance performance of 401 nos. companies out of the sample of BSE 500 Index companies, the Corporate Governance Index (CGI) is constructed based on the raw scores of three important governance variables namely, Board of Directors, Auditor and Audit Committee. The period of empirical study is 2015-16 and the secondary data sources of the study include the annual reports of the sample companies (uploaded in the respective company's websites), Prowess Data Base of Centre for Monitoring of Indian Economy (CMIE), various websites, published data in journals, articles, bulletins etc. The results of the study reveal an overall good corporate governance performance of the sample listed companies.

***KEYWORDS**: BSE 500 Index Companies, Corporate Governance Index (CGI), SEBI (LODR) Regulations, 2015, Audit Committee.*

Introduction

Corporate governance is the matrix of multiple variables aimed at attaining accountability, transparency, independence and fairness in management functions. Though such variables have different dimensions but their common objective is to achieve effective governance for the protection of different stakeholders and the organizational efficiency for better firm performance. The important corporate governance variables include board composition, board size, auditor's independence, size and composition of the audit committee etc. In India, a company is incorporated and comes into operation as per the requirements of the provisions of the Companies Act, 1956. After introduction of the Companies Act, 2013 all companies are governed under this Act subject to applicability of the old Act, viz, the Companies Act, 1956 in some areas where the provisions of the Companies Act, 2013 are not made applicable. A listed company is also required to comply with the requirements of the listing Agreement to remain as a listed company. The Securities and Exchange Board of India (SEBI) is the regulatory authority of the securities market in India. All the stock exchanges of the country are under the control and supervision of SEBI. SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 was notified in the Extraordinary Gazette of India on 02.09.2015 and with the enforcement of these Regulations, 128 nos. circulars issued by SEBI from time to time up to 08.04.2015 were repealed. The corporate governance issues of the listed entities are now governed by the said Regulations. In fact, a listed company is to comply with the stricter provisions of both the Companies Act, 2013 and the SEBI (LODR) Regulations, 2015. In this paper we empirically investigate the standing of the Indian listed companies from the perspective of corporate governance performance. In section 2, review of different literatures on the subject matter is made. Sample and data collection process for the empirical study is

* Professor, Department of Business Administration, University of Kalyani, Kalyani, West Bengal, India.
** Research Scholar, Department of Business Administration, University of Kalyani, Kalyani, West Bengal.

discussed in Section 3. Methodology for ranking of the companies from the corporate governance perspective is discussed in Section 4. In Section 5 the findings and results of the study are stated and Section 6 concludes the study.

Literature Review

Corporate governance is concerned with proper board structure, values, and processes to tackle the changing demands of different stakeholders (including shareholders) in and around an organization. It is directed towards development of a set-up which can appropriately manage the relationships between board, management, major stakeholders (including shareholders) (Garratt, 1996).

Black and Khanna (2007) note the investors' reactions (in May 1999) after the announcement of introduction of clause 49 of the Listing Agreement relating to corporate governance for the Indian listed companies. Introduction of clause 49 is considered as a watershed event in the corporate governance evolution of India. The authors find that the average gain of the large firms is 4.5% (approx.) in comparison to that of small firms over a 3 trading-day event window starting from the announcement date. It is also noticed that faster growing and cross-listed firms are more benefited than other firms.

Brown and Caylor (2004) construct the Gov-Score, a broad measure of corporate governance, which is composed of 51 factors under eight heads: board, audit, and directors' education, compensation of executives and directors, by-laws/charter, state of incorporation, ownership, and progressive practices. The authors find that well governed firms are profitable, more valuable and also can make better cash payout to the shareholders. The study also reveals that executive and directors' compensation are significantly related with good performance. Whereas, charter / by-laws is associated with bad performance. The authors also mention that G-Index,(created by Gompers, Ishii & Metrick, 2003) an off-used summary measure of corporate governance is based on 24 governance factors. The authors also state that the Gov-Score is more associated with firm performance than the G-Index.

Corporate governance of an organization is a multi-dimensional and complex matrix of different internal and external factors. Corporate Governance Index (CCI) considers multiple factors instead of a single one. CGI helps the regulators to assess the progress of corporate governance reforms, the investors to choose a good company for their investment, the companies to review the benefits of adoption of a corporate governance system (Sarkar et al., 2012).There are several types of CGI used in previous empirical studies such as academic, commercial, and self-constructed. Chhaochharia and Laeven (2009) put equal weightage to all the governance variables in construction of CGI. Extant literature indicates that the researchers mostly use the self- constructed indices. The researchers in the self-constructed indices freely choose the sample and use the relevant governance variables for their study. Some Indian authors namely (Sarkar et al., 2012), and (Balasubramanium et al., 2010) have developed such indices.

Sample and Data Collection

In India, the early attempt to impose the corporate governance requirements are made applicable to listed companies (for example, clause 49 of the Listing Agreement is introduced in 2000).The requirements of the Companies Act, 2013 are not comprehensive. Listed companies in India are required to comply with the corporate governance requirements of the Companies Act, 2013 and SEBI (LODR) Regulations, 2015. Accordingly, we concentrate our study on listed companies in India. The Bombay Stock Exchange (BSE)[1] is the oldest stock exchange in India and is still operative .The number of companies listed with BSE is more than that of National Stock Exchange (NSE)[2]. Hence we have first selected the entire sample of BSE 500 Index companies listed with Bombay Stock Exchange. BSE 500 Index[3] companies comprise more than 90% of market capitalization of all BSE listed companies. Out of these 500 companies, 81 companies relating to banks, financial and allied institutions are excluded from our study, because such firms are governed by the regulatory framework, governance practices and administrative systems which are quite different from normal manufacturing firms. Moreover, data relevant for our study for 18 companies are not available. After all these exclusions, finally 401 companies are considered for our empirical study. The details of exclusions are given in Table 1.

These companies are associated with various industries such as metal products, information technology, capital goods, FMCG, power, transport equipments, housing, healthcare, chemicals, petrochemicals, transport services, dairy, electronics, diversified industries etc. For our study we have considered the data of those companies for the financial year 2015-16, the year in which SEBI (LODR) Regulations, 2015 have been implemented. For our study, we have collected data from different secondary sources. Our sources include the annual reports of the sample companies (uploaded in the respective company's websites), Prowess Data Base of Centre for Monitoring of Indian Economy (CMIE), various websites, published data in journals, articles, bulletins etc.

Methodology of Ranking

Consistent with the studies made by (Sarkar et al., 2012; Haldar and Rao, 2013; Mohanty, 2003), we have used Corporate Governance Index (CGI) to measure and rank the corporate governance performance of the sample companies. The CGI is prepared in the Indian context based on available secondary data. In our study we have used three important governance tools such as Board of Directors, Audit Committee and Auditors to denote the overall governance measure (CGI) of a company. The CGI constructed in our study has the aforesaid three sub-indices. The value of each sub-index is computed by putting unweighted scores for each variable included in the respective sub-index. The range of scores of the variables is 0-5. Initially, we calculated actual scores obtained by each of the sample companies by adding the sub-index scores .Thereafter, total scores obtained by a company is divided by maximum scores obtainable i.e. the sum total of variables multiplied by 5.

The formula is shown as:

$$CGI = \frac{\text{Scores obtained}}{\text{Maximum obtainable scores}}$$

The above unweighted index based on raw scores is widely used in various literatures for index construction. Such type of index treats symmetrically all the variables of the sub-indices without any arbitrariness and relative significance of variables which is generally found in the case of preparation of a weighted index (Coles et al., 2003).

Findings and Results

In this section, we present our findings and results on Corporate Governance Index and ranking of sample companies. We have already explained in Section 4, the methods of construction of CGI to measure and rank the corporate governance performance of sample companies. In Table 2, we have given scores of top five companies and the bottom five companies on the basis of their corporate governance ranks. To maintain confidentiality, we are not giving names of the companies but disclosing their ranks on the basis of CGI scores. It is also observed that the overall average CGI of all the sample companies is 0.71. The median value is 0.72 which is near to mean value of the sample companies. The standard deviation of the sample companies from mean value is .073. The overall CGI score ranges between 0.88 to 0.44.

Conclusion

The results of the empirical investigation reveal that the Indian listed companies on an overall basis are good in their corporate governance performance which is evident from the mean and median value of CGI of 0.71 and 0.72 respectively. Both the Companies Act, 2013 and SEBI (LODR) Regulations, 2015 put stringent compliance norms of corporate governance for the Indian listed companies. The regulations based corporate governance practices in India aim at protection of interest of different stakeholders (including shareholders) of listed companies which ultimately leads to the improvement of CGI. In fact, three important governance tools of our study such as Board of Directors, Audit Committee and Auditors play a very key role in protection of stakeholders' (including shareholders) interest in listed companies. With good corporate governance performance, the companies will be able to develop long standing and stronger relationship with the stakeholders due to the high level of trust and confidence on published data of the companies. Similarly, quality governance practices with higher level of transparency, fairness, trust and integrity will help to create an atmosphere conducive to minimization of risks, corruptions and mismanagement. Moreover, the sound governance framework will also help the companies to raise funds from the external sources at a lower cost. It is expected that in future, with the stringent implementation of corporate governance norms through improved regulatory and administrative measures, the Indian listed companies will be able to set a good example for a world class governance system.

Notes

- Bombay Stock Exchange (BSE) is the first and largest securities market in India and was established in 1875. The BSE lists close to 6,000 companies.
- National Stock Exchange (NSE) is the leading stock exchange of India and is located at Mumbai. NSE was established in 1992. NSE's Flagship Index, the NIFTY 50, the 50 stock index is used extensively by investors as barometer of Indian capital markets.

- BSE 500 Index is a free-float weighted index that represents more than 90% of the total market capitalization on BSE India exchange. This index represents all 20 major industries of the economy.

References

- Balasubramanian,N.,Black,B.S., and Khanna,V.(2010). The relation between firm-level corporate governance and market value : A case study of India, *Emerging Markets Review*,*11*, 319-340.
- Black, B.S., and Khanna, V.S. (2007). Can corporate governance reforms increase firm market values? Event study evidence from India. *Journal of Empirical Legal Studies*, *4*, 749-796.
- Brown, L.D., and Caylor, M.L. (2004). Corporate governance and firm performance. Georgia State University Working Paper.
- Chhaochharia,V., and Laeven, L. (2009). Sovereign wealth funds : Their investment strategies and performance. Working paper, International Monetary Fund.
- Coles, J.W., Mc Williams,V.B., and Sen, N. (2003). An examination of the relationship of governance mechanisms to performance. *Journal of Management, 27*(1), 23-50.
- Companies Act, (2013). Available at WWW.mca.gov.in accessed on 26.3.2017
- Garratt, Bob (1996), *The Fish Rats from the Head.* Profile Books, London.
- Gompers,P.A., Ishii, J.L., and Metrick, A. (2003). Corporate governance and equity prices. *Quarterly Journal of Economics, 118* (1), 107-155.
- Haldar, A., and Rao, N, (2013). Governance practices of Indian Firms: An empirical analysis. *The Empirical Economic Letters, 12*(9).
- Mohanty,P.(2003). Institutional investors and corporate governance of India, conference paper at fifteenth AIMS conference held at XIM, Bhubaneswar .
- Sarkar, J., Sarkar, S., and Sen, K. (2012). Analysis of a corporate governance index for large listed companies in India. *Indian Accounting Review, 16* (1), 1-18.
- Sebi LODR Regulations,(2015). Available at www.sebi.gov.in accessed on 27.3.2017.

Table 1: Details of Sample and Exclusions

Particulars		No. of Companies
Initial sample size		500
Less: Companies relating to banks, financial institutions/organizations:		
Data relevant for study not available	81	
Final sample size for study	18	99
		401

Table 2: CGI of the Best & the Worst Performances

Panel -1	
Rank of the company	Overall CGI
Company - 1	0.88
- 2	0.88
- 3	0.87
- 4	0.86
- 5	0.85
Average	0.868
Company - 397	0.53
- 398	0.52
- 399	0.52
- 400	0.50
- 401	0.44
Average	0.502
Panel -2	
Mean	0.71
Median	0.72
Standard Deviation	0.073
Skewness	-.0.40
Kurtosis	0.068

Source: Own computation