



**THE QUALITY OF CORPORATE GOVERNANCE PRACTICES IN
MANUFACTURING SECTOR IN INDIA - AN EMPIRICAL
INVESTIGATION**

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ABSTRACT

Purpose: An analysis of quality of corporate governance practices in manufacturing sector in India. **Design/Methodology/Approach:** The study is based on signaling theory according to which if a firm is having better governance it will emit signal by disclosing its business activities in order to get competitive advantage. For the purpose, secondary data related to corporate governance practices has been

collected for four years (From 2011 to 2014). The analysis has been done using scorecard method developed by Dr S. C. Das in 2007. **Findings:** The corporate governance practices of Indian manufacturing sector is not satisfactory. **Practical implications:** The quality of governance practices in Indian manufacturing sector point out the need to look at their governance in a more nuanced manner. The exiting legislations need amendments because they are unable to control such dubious activities. **Originality/value:** The comparative analysis of quality of governance practices among Indian manufacturing firms using scorecard has not been done so far.

KEYWORDS: Corporate governance; Scorecard; Manufacturing.

INTRODUCTION

Corporate governance in broader sense describes processes, customs, policies, laws and institutions that direct organizations or corporations in which way they should administer and

control their operations. The corporate governance means governance of a firm should be in such a way that it provide justice to all the stakeholders. There are various benefits associated with good governance like it provide standard for establishing striking investment environment to gain competitive advantage over other firms. Further, good corporate governance is fundamental to economies with extensive business background and facilitates success for entrepreneurship, it improves strategic thinking at the top, it rationalizes the management and monitoring of risk that a firm faces globally, it limits the liability of top management and directors, it assures the integrity of financial reports and it also has long term reputational effects among key stakeholders. There are mainly two corporate governance issues one is principle-agent problem where managers act as agent and owner act as principle. The separation of ownership from control is the core of the agency problems facing by the firms (Berle and Means, 1932; Jensen and Meckling, 1976). Another issue is exploitation of minority shareholders by domineering shareholders.

An effective corporate governance system is one where the board performs its dual functions efficiently. The board of directors (BOD) of a company directs and controls the management of a company and is accountable towards shareholders. There are various dimensions of board. One of the significant dimensions is board's composition. The board is composed of promoters, executive directors and non-executive directors and independent director. The independent directors are those directors who apart from receiving director's remuneration do not have any other material pecuniary relationship with company. Further, all pecuniary relationship or transactions of the non executive directors should be disclosed in the annual report. As per exiting legislation in case a company has a non-executive chairman, at least one third of board should comprise of independent directors and in case a company has an executive chairman at least half of board should be independent. The nominee directors are nominees of the financial institutions to safeguard their interest it may be present of retired employee of financial institution or outsiders. The committee recommend that institutions should appoint nominees on the boards of companies only on a selective basis where such appointment is pursuant to a right under loan agreements as where such appointment in is considered necessary to protect like interest of the institutions.

The audit committee should set up with minimum three members, all being non-executive directors, with the majority being independent and with at least one director having financial and accounting knowledge. The audit committee should meet at least thrice a year. One

meeting must be held before finalization of annual accounts and one necessarily every six months. The audit committees have been empowered by giving a list of power to the committee like owners of audit committee (Mandatory) are to investigate any activity within its terms of reference, can seek information from any employee, can obtain outside legal or other professional advice, can secure attendance of outsiders with relevant expertise if it considers necessary. The audit committee should perform following functions it should ensure that the financial statement is correct, sufficient and creditable, should recommend the appointment and removal of external audit, should review management annual financial statement before submission to board related to changes in accounting policies and practices, it should review with the management about adequacy of control, it should discuss with internal auditors into the matter suspecting fraud or irregularity, it should discuss with external auditors before the audit commences and also post-audit discussion to ascertain any area of concern.

RESEARCH METHODOLOGY AND SAMPLE DESIGN

This paper is a comparative analysis of status of corporate governance practices among four manufacturing firms during four years from 2011 to 2014. The data has been collected from Prowess database. This resulted in 961 companies from the manufacturing sector. All banks and financial services companies were eliminated from the list as banks are exempted from disclosure of corporate governance. Further, state-owned enterprises (public sector undertakings) were also exempted from disclosing transactions with other government enterprises, and hence were not included in the sample. The data is collected from corporate governance reports of sample firms.

RESULTS AND DISCUSSION

Statement of Company's philosophy on code of governance

In the industry there are 4 companies, while looking to the Corporate Governance, the first score point was statement of Company's philosophy on Corporate Governance and thus the point was assigned a weightage of 2 on a scale of 100. All 4 companies get the expected score of 2. All companies have sufficient disclosure of the statement of Company's philosophy on code of governance.

Structure and Strength of board

In the Corporate Governance score, the second score point was about the Structure and Strength of the board. The point was assigned a weightage of 2 on a scale of 100. All 4

companies get the expected score of 2. All companies have sufficiently disclosed the composition of the Board of Directors.

Chairman & CEO Duality

The appointment of Chairman of the board carries of critical importance. The third point describes about the duality of Chairman and CEO. The point assigned a weightage of total 5 points, which are assigned on the following basis. AIA ENGINEERING LTD, ADANI enterprise and ACC among these companies has assigned a score of 5. However, ABB firm scored 4 points.

Disclosure of Tenure and Age limit of directors

In the Corporate Governance score, the fourth point was about Disclosure of Tenure and Age limit of directors. The point was assigned a weightage of 2 on a scale of 100. The disclosures about the tenure and age limit of directors are sufficiently available in the annual report of the all companies.

Post Board meeting follow up system and compliance of the board procedures

In the Corporate Governance score, the sixth point was about disclosure of Post Board meeting follow up system and compliance of the board procedures. The point was assigned a weightage of 2 on a scale of 100. The systematic disclosures about the Post Board meeting follow up system are sufficiently available in the annual report of the AIA and ACC whereas it is not sufficiently available in ABB and ADANI. Hence, 2 companies get 1 point in this section and 2 companies get 2 points in this section.

The appointment of lead independent director

The point was assigned a weightage of 2 on a scale of 100. Among the companies, AIA and ACC have formally appointed lead independent director and the rest of the companies have not appointed lead independent director. Hence, AIA and ACC get 2 points and rest of the companies gets 1 point in this section.

Disclosure of other provision as to the boards and committees

In the Corporate Governance score, the eighth point was about the disclosure of other provision as to the boards and committees. The point was assigned a weightage of 1 on a scale of 100. It is observed that 3 companies have sufficiently disclosed about the various

committees and sub-committees of the board except. Hence, another company i.e. AIA get expected score of 1 where as ACC, ABB and ADANI get 2 points.

Disclosure of Remuneration Policy & Remuneration of Directors

In the Corporate Governance score, the ninth point was about the disclosure of Remuneration Policy & Remuneration of Directors. The point was assigned a weight age of 2 on a scale of 100. The point was further equally divided into two points, (i) Disclosure of remuneration policy and (ii) Disclosure of remuneration to directors. All companies have sufficiently disclosed about remuneration to directors except.

Code of Conduct

In the Corporate Governance score, the tenth point was about the code of conduct. The point was assigned a weightage of 2 on a scale of 100. The point was further equally divided into two points, (i) Information on Code of Conduct and (ii) Affirmation regarding compliance for code of conduct. It is observed that all the companies have sufficiently disclosed about both the above points. All 4 companies only 1 get expected score of 2.

Board Committees

In the Corporate Governance score, the eleventh point is about the various Committees of the board. The point carries a weightage of 25 on a scale of 100. The sub classification of the point is as under. (i) Audit Committee 8 (ii) Remuneration Committee 6 (iii) Shareholders' / Investors Grievance Committee 5 (iv) Nomination Committee 2 (v) Other Committees 4.

Audit Committee

The Audit Committee is assigned a weightage of 8. It is observed that all companies have made sufficient disclosure about the audit committee. All companies have sufficiently disclosed committee charter and terms of reference. However, none of the companies have scored completely and none have published Audit Committee Report in the annual report.

Remuneration / Compensation Committee

The Remuneration/Compensation Committee is assigned a weightage of 6. It is observed that all companies have formed the committee. They have also made sufficient disclosure. None of the companies have published Remuneration Committee Report in the annual report except.

Shareholders' / Investors Grievance Committee

The Shareholders' / Investors Grievance Committee are assigned a weightage of 5. It is observed that all the sample companies have formed the committee. However, none of the companies have published information about the investors / shareholders' survey (if conducted).

Table 1: Score Card for Year 2011.

Source: S. C. Das, 2007.

No.	Governance Parameters	Scores Assigned	AIA ENGINEERING LTD.	ACC LTD.	ABB LTD.	ADANI ENTERPRISE LTD.
1	Statement of Company's philosophy on code of governance	2	2	2	2	2
2	Structure and Strength of board	2	2	2	2	2
3	Chairman & CEO Duality	5	5	5	4	5
4	Disclosure of Tenure and Age limit of directors	2	1	2	2	2
5	Disclosure of definition of Independent Director and Financial Expert and also selection Criteria of Board of Directors including independent directors	3	2	3	2	2
6	Post Board meeting follow up system and compliance of the board procedures	2	2	2	2	2
7	Appointment of lead independent director	2	2	2	2	2
8	Disclosure of other provision as to the boards and committees	1	0	1	1	1
9	Disclosure of Remuneration Policy & Remuneration of Directors	2	1	2	2	1
10	Code of Conduct	2	2	2	2	2
11	Board Committee	25	20	25	22	23
12	Disclosure and Transparency	25	18	23	20	20

13	General Body Meetings	3	2	3	3	3
14	Means of communication and General shareholder information	2	2	2	2	2
15	CEO / CFO Certification	2	2	2	2	2
16	Compliance of corporate governance and auditor's certificate	10	7	9	8	8
17	Disclosure of Stakeholders' interests	10	6	10	7	8
	TOTAL	100	78	96	85	88
	Company Corporate Governance Scores					

Table 2: Score Card for Year 2012

Source: S. C. Das, 2007

No.	Governance Parameters	Scores Assigned	AIA ENGINEERING LTD.	ACC LTD.	ABB LTD.	ADANI ENTERPRISE LTD.
1	Statement of Company's philosophy on code of governance	2	2	2	2	2
2	Structure and Strength of board	2	2	2	2	2
3	Chairman & CEO Duality	5	5	5	4	5
4	Disclosure of Tenure and Age limit of directors	2	2	2	2	2
5	Disclosure of definition of Independent Director and Financial Expert and also selection Criteria of Board of Directors including independent directors	3	1	2	1	1
6	Post Board meeting follow up system and compliance of the board procedures	2	1	1	1	1
7	Appointment of lead independent director	2	2	2	1	2
8	Disclosure of other provision as to the boards and committees	1	1	2	2	2
9	Disclosure of Remuneration Policy & Remuneration of Directors	2	2	2	2	2
10	Code of Conduct	2	2	2	1	1
11	Board Committee	25	19	24	18	20

12	Disclosure and Transparency	25	16	23	20	24
13	General Body Meetings	3	2	3	3	3
14	Means of communication and General shareholder information	2	1	2	1	1
15	CEO / CFO Certification	2	1	2	1	1
16	Compliance of corporate governance and auditor's certificate	10	7	9	9	8
17	Disclosure of Stakeholders' interests	10	6	9	8	8
	TOTAL	100	72	94	77	83
	Company Corporate Governance Scores					

Table 3: Score Card for Year 2013

Source: S. C. Das, 2007

No.	Governance Parameters	Scores Assigned	AIA ENGINEERING LTD.	ACC LTD.	ABB LTD.	ADANI ENTERPRISE LTD.
1	Statement of Company's philosophy on code of governance	2	2	2	2	2
2	Structure and Strength of board	2	2	2	2	2
3	Chairman & CEO Duality	5	5	5	4	5
4	Disclosure of Tenure and Age limit of directors	2	2	2	2	2
5	Disclosure of definition of Independent Director and Financial Expert and also selection Criteria of Board of Directors including independent directors	3	1	2	1	1
6	Post Board meeting follow up system and compliance of the board procedures	2	1	1	1	1
7	Appointment of lead independent director	2	2	2	1	2
8	Disclosure of other provision as to the boards and committees	1	1	2	2	2
9	Disclosure of Remuneration Policy & Remuneration of Directors	2	2	2	2	2
10	Code of Conduct	2	1	2	1	1
11	Board Committee	25	18	25	20	21
12	Disclosure and Transparency	25	16	22	21	24
13	General Body Meetings	3	2	3	3	3
14	Means of communication and General shareholder information	2	1	2	1	1
15	CEO / CFO Certification	2	1	2	1	1

16	Compliance of corporate governance and auditor's certificate	10	7	10	9	8
17	Disclosure of Stakeholders' interests	10	6	9	8	8
	TOTAL	100	70	95	80	84
	Company Corporate Governance Scores					

Table 4: Score Card for Year 2014

Source: S. C. Das, 2007

No.	Overnance Parameters	Scores Assigned	AIA ENGINEERING LTD.	ACC LTD.	ABB LTD.	ADANI ENTERPRISE LTD.
1	Statement of Company's philosophy on code of governance	2	2	2	2	2
2	Structure and Strength of board	2	2	2	2	2
3	Chairman & CEO Duality	5	5	5	4	5
4	Disclosure of Tenure and Age limit of directors	2	2	2	2	2
5	Disclosure of definition of Independent Director and Financial Expert and also selection Criteria of Board of Directors including independent directors	3	1	2	1	1
6	Post Board meeting follow up system and compliance of the board procedures	2	1	1	2	2
7	Appointment of lead independent director	2	2	2	1	1
8	Disclosure of other provision as to the boards and committees	1	1	2	2	2
9	Disclosure of Remuneration Policy & Remuneration of Directors	2	2	2	2	2
10	Code of Conduct	2	1	2	1	1
11	Board Committee	25	18	25	20	21
12	Disclosure and Transparency	25	16	23	21	24
13	General Body Meetings	3	2	3	3	3
14	Means of communication and General shareholder information	2	0	2	1	1
15	CEO / CFO Certification	2	1	2	1	1

16	Compliance of corporate governance and auditor's certificate	10	6	10	9	8
17	Disclosure of Stakeholders' interests	10	6	9	8	8
	TOTAL	100	68	96	81	84
	Company Corporate Governance Scores					

CONCLUSION

All 4 companies get the expected score of 2. All companies have sufficient disclosure of the statement of Company's philosophy on code of governance. In the Corporate Governance score, the second score point was about the Structure and Strength of the board. The point was assigned a weightage of 2 on a scale of 100. All 4 companies get the expected score of 2. All companies have sufficiently disclosed the composition of the Board of Directors. The appointment of Chairman of the board carries of critical importance. The third point describes about the duality of Chairman and CEO. The point assigned a weightage of total 5 points, which are assigned on the following basis. AIA ENGINEERING LTD, ADANI enterprise and ACC among these companies has assigned a score of 5. However, ABB firm scored 4 points. In the Corporate Governance score, the fourth point was about Disclosure of Tenure and Age limit of directors. The point was assigned a weightage of 2 on a scale of 100. The disclosures about the tenure and age limit of directors are sufficiently available in the annual report of the all companies. In the Corporate Governance score, the sixth point was about disclosure of Post Board meeting follow up system and compliance of the board procedures. The point was assigned a weightage of 2 on a scale of 100. The systematic disclosures about the Post Board meeting follow up system are sufficiently available in the annual report of the AIA and ACC whereas it is not sufficiently available in ABB and ADANI. Hence, 2 companies get 1 point in this section and 2 companies get 2 points in this section. The point was assigned a weightage of 2 on a scale of 100. Among the companies, AIA and ACC have formally appointed lead independent director and the rest of the companies have not appointed lead independent director. Hence, AIA and ACC get 2 points and rest of the companies gets 1 point in this section. In the Corporate Governance score, the eighth point was about the disclosure of other provision as to the boards and committees. The point was assigned a weightage of 1 on a scale of 100. It is observed that 3 companies have sufficiently disclosed about the various committees and sub-committees of the board except. Hence, another company i.e. AIA get expected score of 1 where as ACC, ABB and ADANI get 2 points. In

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