
Role of SEBI in Promoting Corporate Governance: A Conceptual paper

Ms. Amita Rani

Associate professor

University School of Management Studies

Rayat Bahra University, Mohali

Introduction

Securities and Exchange Board of India was formed after the Indian parliament passed Securities and Exchange Board of India Act, 1992 in response to financial Services Assessment program, a program developed by the World Bank and International Monetary Fund that observes and reports on global financial systems. The Indian government wanted to establish a strong financial atmosphere and securities market with a regulator promoting the latest in corporate governance standards. SEBI sets standards in which the securities market must operate, protecting the rights of issuers and investors. SEBI has power to investigate circumstances where market or its players have been harmed and can enforce govern standards with directives. An appeal process in place ensures accountability and transparency. SEBI may terminate from the securities list any company that does not comply with its governance standards and regulation. Main aim of its origin was to curb the malpractices such as Lack of transparency in the trading operations and prices charged to clients, Poor services due to delay in passing contract notes or not passing contract notes, Delay in making payments to clients or in giving delivery of shares, Persistence of odd lots and refusal of companies to stop this practice of allotting shares in odd lots, Insider trading by agents of companies or brokers rigging and manipulating prices, unofficial premium on new issue, violation of rules and regulations of stock exchange and listing requirements. Due to these malpractices the customers started losing confidence and faith in stock exchange. Many high profile corporate governance failure scams like the stock market scam, the UTI scam, Ketan Parikh scam, Satyam scam, which was severely criticized by the shareholders, called for a need to make corporate governance in India transparent as it greatly affects the development of the country. Effective corporate governance is only key to regain the trust of investors and safeguard their interest.

Main Objectives of SEBI:

The SEBI has been entrusted with both the regulatory and developmental functions. The objectives of SEBI are as follows:

- a. Investor protection, to ensure steady flow of savings into the Capital Market.
- b. Ensuring the fair practices by the issuers of securities, namely, companies so that they can raise resources at least cost.
- c. Promotion of efficient services by brokers, merchant bankers and other intermediaries so that they become competitive and professional.

Corporate Governance

Corporate governance is the manner in which companies or market systems operate, including the rules, regulations, policies and standards for accountability, transparency and general corporate integrity. Corporate governance has also been more narrowly explained as a set of law and sound approaches by which corporations are directed and controlled while focusing on the internal and external corporate structures with

the intention of monitoring the actions of management and directors and thereby, mitigating agency risks which may stem from the misdeeds of corporate officers.

Corporate Governance: Conceptual Framework

Corporate Governance has gained momentum across the world due to corporate failures, unethical business practices and insufficient disclosure etc. Effective Corporate Governance depends upon two factors. Transparency in the business operations and the second are the legal and regulatory framework created by the Government. There is a gap between percept and practice of Corporate Governance. The topic of Corporate Governance has gained prominence since the 1980's and more so after the code of corporate governance issued by the Cadbury committee. In line with the Cadbury committee, the Kumara-mangalam Birla Committee has also issued a code of corporate governance for companies in India. According to the Kumara mangalam Birla Committee, **“Corporate governance is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders' role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board's actions are subject to laws, regulations and the shareholders in general meeting”**. The governance structure of a country protects the investors from expropriation by managers and large shareholders. In different jurisdictions, rules protecting investors come from different sources, including company, security, bankruptcy, takeover, and competition laws, and also from stock exchange regulations and accounting standards (La Porta et al 2000).

Legal and Regulatory framework on corporate governance

The Indian statutory framework has, by and large, been in consonance with the international best practices of corporate governance. Broadly speaking, the corporate governance mechanism for companies in India is enumerated in the following enactments/ regulations/ guidelines/ listing agreement:

1. **Companies Act, 1956** provides for basic framework for regulation of all the companies. But it had some loopholes which could not control fraudulent practices and raised a question mark on corporate governance practices of the concern. So, there are number of amendment had proposed and implemented in the Act. But after the Satyam scam need realised to reframe the Act, which resulted in Companies Act, 2013.

The Companies Act, 2013 inter alia contains provisions relating to board constitution, board meetings, board processes, independent directors, general meetings, audit committees, related party transactions, disclosure requirements in financial statements, etc.

2. **Securities and Exchange Board of India (SEBI) Guidelines:** SEBI is a regulatory authority having jurisdiction over listed companies and which issues regulations, rules and guidelines to companies to ensure protection of investors.

3. **Standard Listing Agreement of Stock Exchanges:** For companies whose shares are listed on the stock exchanges.

4. **Accounting Standards issued by the Institute of Chartered Accountants of India (ICAI):** ICAI is an autonomous body, which issues accounting standards providing guidelines for disclosures of financial information. Section 129 of the New Companies Act inter alia provides that the financial statements shall give a true and fair view of the state of affairs of the company or companies, comply with the accounting standards notified under s 133 of the New Companies Act. It is further provided that items contained in such financial statements shall be in accordance with the accounting standards.

5. **Secretarial Standards issued by the Institute of Company Secretaries of India (ICSI):** ICSI is an autonomous body, which issues secretarial standards in terms of the provisions of the New Companies Act. So far, the ICSI has issued Secretarial Standard on "Meetings of the Board of Directors" (SS-1) and

Secretarial Standards on "General Meetings" (SS-2). These Secretarial Standards have come into force w.e.f. July 1, 2015. Section 118(10) of the New Companies Act provide that every company (other than one person company) shall observe Secretarial Standards specified as such by the ICSI with respect to general and board meetings.

Role of SEBI in promoting Corporate Governance

The establishment of SEBI has also played a significant role in establishing norms for corporate governance in India. Over the years, SEBI constituted two committees to make recommendations relating to corporate governance in india, which were Kumar Manglam Birla committee, which submitted its report in 2000 and the Narayana Murthy Committe, which submitted its report in 2003. These committees made various important recommendations. SEBI Major Recommendations were:

-) Composition of Board
-) Formation of Audit Committee
-) Disclosure of relevant information to the shareholders

The recommendations of these committees form the foundation of the legal regime for corporate governance in India. An improved corporate governance is the key objective of the regulatory framework in the securities market. Accordingly, **Securities and Exchange Board of India (SEBI)** has made several efforts with a view to evaluate the adequacy of existing corporate governance practices in the country and further improve these practices. It is implementing and maintaining the standards of corporate governance through the use of its legal and regulatory framework, namely:-

Securities Contracts (Regulation) Act, 1956

This Act was enacted to prevent undesirable transactions and to check speculation in the securities by regulating the business of dealing therein. Any stock exchange, which is desirous of being recognised, may make an application in the prescribed manner to the Central Government. Every application shall contain such particulars as may be prescribed, and shall be accompanied by a copy of the bye-laws of the stock exchange for the regulation and control of contracts as well as a copy of the rules relating in general to the constitution of the stock exchange, and in particular to; firstly, the governing body of such stock exchange, its constitution and powers of management and the manner in which its business is to be transacted; secondly, the powers and duties of the office bearers of the stock exchange; thirdly, the admission into the stock exchange of various classes of members, the qualifications for membership, and the exclusion, suspension, expulsion and re-admission of members there from or there into; fourthly, the procedure for the registration of partnerships as members of the stock exchange, in cases where the rules provide for such membership; and the nomination and appointment of authorised representatives and clerks. Every recognised stock exchange shall furnish the Central Government with a copy of the annual report, and such annual report shall contain such particulars as may be prescribed. It may make rules or amend any rules made by it to provide for all or any of the following matters, namely:- (i) the restriction of voting rights to members only in respect of any matter placed before the stock exchange at any meeting; (ii) the regulation of voting rights in respect of any matter placed before the stock exchange at any meeting so that each member may be entitled to have one vote only, irrespective of his share of the paid-up equity capital of the stock exchange; (iii) the restriction on the right of a member to appoint another person as his proxy to attend and vote at a meeting of the stock exchange; etc.

If, in the opinion of the Central Government, an emergency has arisen and for the purpose of meeting the emergency, the Central Government considers it expedient so to do, it may, by notification in the Official Gazette, for reasons to be set out therein, direct a recognised stock exchange to suspend such of its business for such period not exceeding seven days and subject to such conditions as may be specified in the notification, and, if, in the opinion of the Central Government, the interest of the trade or the public interest requires that the period should be extended, it may, by like notification extend the given period from time to time. Securities Contracts (Regulation) Amendment Act, 2007 has been enacted in order to further amend the Securities Contracts (Regulation) Act, 1956, with a view to include securitisation instruments under the

definition of 'securities' and provide for disclosure based regulation for issue of the securitised instruments and the procedure thereof. This has been done keeping in view that there is considerable potential in the securities market for the certificates or instruments under securitisation transactions. Further, replication of the securities markets framework for these instruments would facilitate trading on stock exchanges and, in turn, help development of the market in terms of depth and liquidity.

Securities and Exchange Board of India Act, 1992

This Act was enacted to protect the interests of investors in securities and to promote the development of, and to regulate, the securities market and for matters connected therewith or incidental thereto. For this purpose, the SEBI (the Board), by regulation, specify:- (i) the matters relating to issue of capital, transfer of securities and other matters incidental thereto; and (b) the manner in which such matters shall be disclosed by the companies. No stock-broker, sub-broker, share transfer agent, banker to an issue, trustee of trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and such other intermediary who may be associated with securities market shall buy, sell or deal in securities except under, and in accordance with, the conditions of a certificate of registration obtained from the Board in accordance with the regulations made under this Act.

No depository, participant, custodian of securities, foreign institutional investor, credit rating agency, or any other intermediary associated with the securities market as the Board may by notification in this behalf specify, shall buy or sell or deal in securities except under and in accordance with the conditions of a certificate of registration obtained from the Board in accordance with the regulations made under this Act. Further, no person shall sponsor or cause to be sponsored or carry on or caused to be carried on any venture capital funds or collective investment scheme including mutual funds, unless he obtains a certificate of registration from the Board in accordance with the regulations. Every application for registration shall be in such manner and on payment of such fees as may be determined by regulations. The Board may, by order, suspend or cancel a certificate of registration in a prescribed manner, as may be determined by regulations under this Act. However, no order shall be made unless the person concerned has been given a reasonable opportunity of being heard.

Depositories Act, 1996

This Act was enacted to provide for regulation of depositories in securities and for matters connected therewith or incidental thereto. It provides for the introduction of scripless trading system and settlement, which is considered necessary for the effective functioning of the securities markets. As per the Act, the term 'depository' means "a company formed and registered under the Companies Act, 1956 and which has been granted a certificate of registration under sub-section (1A) of section 12 of the Securities and Exchange Board of India Act, 1992". No depository shall act as a depository unless it obtains a certificate of commencement of business from the Board (the SEBI). The Board shall grant a certificate only if it is satisfied that the depository has adequate systems and safeguards to prevent manipulation of records and transactions. However, a certificate shall not be refused unless the depository concerned has been given a reasonable opportunity of being heard. A depository shall enter into an agreement with one or more participants as its agent, in such form as may be specified by the bye-laws. Any person, through a participant, may enter into an agreement, in such form as may be specified by the bye-laws, with any depository for availing its services. Any such person shall surrender the certificate of security, for which he seeks to avail the services of a depository, to the issuer in such manner as may be specified by the regulations. The issuer, on receipt of certificate of security, shall cancel the certificate of security and substitute in its records the name of the depository as a registered owner in respect of that security and inform the depository accordingly. A depository shall, on receipt of information, enter the name of the person referred in its records, as the beneficial owner.

On receipt of intimation from a participant, every depository shall register the transfer of security in the name of the transferee. If a beneficial owner or a transferee of any security seeks to have custody of such security, the depository shall inform the issuer accordingly. Every person subscribing to securities offered by an issuer shall have the option either to receive the security certificates or hold securities with a depository. Where a

person opts to hold a security with a depository, the issuer shall intimate such depository the details of allotment of the security, and on receipt of such information the depository shall enter in its records the name of the allottee as the beneficial owner of that security. A depository shall be deemed to be the registered owner for the purposes of effecting transfer of ownership of security on behalf of a beneficial owner. However, it shall not have any voting rights or any other rights in respect of securities held by it. The beneficial owner shall be entitled to all the rights and benefits and be subjected to all the liabilities in respect of his securities held by a depository. The Board, on being satisfied that it is necessary in the public interest or in the interest of investors so to do, may, by order in writing, (i) call upon any issuer, depository, participant or beneficial owner to furnish in writing such information relating to the securities held in a depository as it may require; or (ii) authorise any person to make an enquiry or inspection in relation to the affairs of the issuer, beneficial owner, depository or participant, who shall submit a report of such enquiry or inspection to it within such period as may be specified in the order.

Major steps to ensure effective corporate governance:

The Companies Act, 2013 was enacted on August 30, 2013 which provides for a major overhaul in the Corporate Governance norms for all companies. The rules pertaining to Corporate Governance were notified on March 27, 2014. SEBI decided to review the provisions of the Listing Agreement in this regard with the objectives to align with the provisions of the Companies Act, 2013, adopt best practices on corporate governance and to make the corporate governance framework more effective. Hence, Clause 35B and Clause 49 of the Equity Listing Agreement have been replaced by new listing agreement. This article highlights the major changes :

Amendments in Clause 35B

This clause is applicable to all listed companies. As per revised clause the Company shall provide e-voting facility to its shareholders, in respect of all shareholders' resolutions, to be passed at General Meetings or through postal ballot. Such e-voting facility shall be kept open for such period specified under the Companies (Management and Administration) Rules, 2014 for shareholders to send their assent or dissent. The Company shall continue to enable those shareholders, who do not have access to e – voting facility, to send their assent or dissent in writing on a postal ballot. The Company shall utilize the service of any one of the agencies providing e-voting platform, which is in compliance with conditions specified by the MCA, Government of India, from time to time. Issuer shall mention the Internet link of such e-voting platform in the notice to their shareholders.

Amendments in Clause 49

The Clause 49 of the Listing Agreement shall be applicable to all companies whose equity shares are listed on a recognized stock exchange from 1st October, 2014. The provisions relating to constitution of a Risk Management Committee shall be applicable to top 100 listed companies by market capitalization as at the end of the immediate previous financial year. The provisions with regards to the Related Party Transactions shall be applicable to all prospective transactions. The main objectives of the amendment was to align the provision of listing agreement with Companies Act, 2013. This is Clause 49(I) of the Listing Agreement. It states the purpose for which the Clause 49 is instated. In case of any ambiguity, the provisions of Clause 49 shall be interpreted and applied in alignment with these principles. Main objectives of the clause are:

-) The Rights of Shareholders
-) Role of stakeholders in Corporate Governance
-) Disclosure and transparency
-) Responsibilities of the Board
-) Board of Directors (“BOD” or “Board”)

The clause 49 is divided into different subsection and each subsection provide a different guideline for effective governance; clause 49 (i) under this section SEBI defines the rights of various stake holders and duty of corporate to protect shareholder's interest. It also explains the duties and responsibilities of board of directors. This specifies that the disclosures must be made regarding proper compliance of prescribed standards of accounting, financial and non- financial disclosure and be transparent Board of Directors. clause 49 (ii) specifies the composition of board, inclusion of restrictions on independent directors, the tenure of independent directors, corporate code of conduct and whistle blowing policy. Clause 49 (iii) defines the constitution of audit committee. The audit committee should have at least 3 members and out of which 2/3rd members be independent directors. All the members must be financially literate and one member must be an expert in accounting or related financial management. This committee has to sit at least 4 times in a year with a gap of not more than four months in between two meetings. Through this amendment, SEBI specifies the powers, role and responsibilities of audit committee members. Nomination and Remuneration committee. Clause 49 (iv) explains the composition of remuneration committee. This clause states the role of the Committee which includes formulation of criteria to evaluate Independent directors, policy devising on Board diversity, identifying prospective directors and senior management in accordance with the criteria laid down, recommendation to the Board policies relating to remuneration of directors and other employees including key managerial personnel. Clause 49 highlighted the responsibilities of listed and unlisted subsidiaries of listed holding companies. Provisions as to unlisted subsidiary company: (a) at least one independent director of the holding company should be director on the board of Director of materially un-listed Indian subsidiary company, (b) the audit committee of the listed holding has to review the financial statements materially un-listed Indian subsidiary company. Clause 49 (vi) specifies that SEBI makes it an obligation of BOD of the top 100 companies by market capitalization to constitute the risk management committee and has to determine its role and functions and delegate powers as it may deem fit. Clause 49 (vii) explains that the companies requires to place, all the information on the related party transactions in the ordinary course of business, periodically in summary form, before the audit committee. Clause 49 (viii), is related with disclosure norms. Companies has to quarterly report disclosing details on all material facts related party transactions along with compliance report on Corporate Governance be disclosed on its website and a web link stated in its annual reports. Apart from it, any change in accounting treatment, information on the remuneration of Directors, directors' relationship with the company are be disclosed along with the annual report. Then material facts on proceeds from public issue, rights issue, and preferential issues must be disclosed and Certification from Chief Executive Officer (CEO) and Chief Finance Officer (CFO). Clause 49 (ix), made Board of Directors and Chief Executive Officer and Chief Finance Officer more accountable and responsible. They must certify that they have reviewed the financial statements and the cash flow statements to the best of their knowledge. Then they have to certify that the Company hasn't entered into any transaction which is a violation of Company's Code of Conduct, illegal or fraudulent to the best of their knowledge. Again it will be their duty to inform the Auditors and Audit committee on any significant changes made in internal control over financial reporting, changes in accounting policies, cases of significant fraud that they have come across. Clause 49 (x) and (xi) specifies that corporate has to obtain the Compliance Certificate on Corporate Governance from the Auditor of the Company or from a Practicing Company Secretary. Such certificate shall become separate part of Annual Report. Certificate is also to be submitted to Stock Exchange along with the Annual Report.

Conclusion

Although SEBI is a young institution but it has been fairly successful in fulfilment of its mandate as capital market regulator, ensuring protection of various stakeholders and increasing participation in capital formation. As per the need arise, SEBI has taken steps to ensuring fair trading and investor protection. SEBI plays a vital role in compliance of governance by corporate. A company that has good corporate governance has a much higher level of confidence amongst the shareholders associated with that company. Active and independent directors contribute towards a positive outlook of the company in the financial market, positively influencing share prices. Corporate Governance is one of the important criteria for foreign institutional investors to decide on which company to invest in. The corporate practices in India emphasize the functions of audit and finances

that have legal, moral and ethical implications for the business and its impact on the shareholders. Amendments introduced by SEBI in Clause 49 roved innovative measures to appropriately balance legislative and regulatory reforms for the growth of the enterprise and to increase foreign investment. The rules and regulations are measures that increase the involvement of the shareholders in decision making and introduce transparency in corporate governance, which ultimately safeguards the interest of the society and shareholders. Corporate governance safeguards not only the management but the interests of the stakeholders as well and fosters the economic progress of India in the roaring economies of the world.

References:

1. Cadbury Adrain, "Report on the Financial Aspects of Corporate Governance," 1992, p.137.
2. Datta , S., "Role of Corporate Governance, " Chartered Secretary, Vol.XXVIII, No. 9, September 1998, pp. 849 - 51.
3. Daryal, V., and Sehgal, V.K., Corporate Governance in India --- AChallenge Before Different Players, Edited book by Singh, D., and Garg, S..First Edition, wheeler Publishing, New Delhi, 2000, pp. 46-47.
4. Gopalswamy, N., "Corporate Governance : The New Paradigm," Wheeler Publishing, New Delhi, 2002, pp. 64-65.
5. Ghosh , T. P., "The Role of Chartered Accountants -- The three pillars of Wisdom," The chartered Accountant, August 2000, pp. 13-20.
6. Israni, S.D., "It's Time for Better Governance," The Economic Times, 9 December 2000, p.5.
7. Lobwo, Samir, Kr., "Corporate Governance: Role of the Board of Directors,"The Management Accountant, Vol.35, No. 10, October 2000, pp. 770 – 73 .
8. Mayer Cohn , " Financial systems and Corporate Governance : A Review of International Evidence," Journal of institutional and Theoretical Economics, Vol. 154, No.1, 1998, pp . 45 – 55.
9. Monte, D. S., "Corporate Governance -- Role of Professionals," Chartered secretary, May 1997, pp.520 –21
10. Naughton, T., " Corporate Governance : An International Perspective," The ICFAI Journal of Corporate Governance, Vol.II, No.3, July 2003, P.90.
11. Pati, A.P., and Moharana, S., "Redefining the Role of Major players in Corporate Governance," The Indian Journal of Commerce, Vol.51, no. 4, October - December 1998, pp373 – 85.
12. Sharma, V.V.S and Shankarraiah, A., "Corporate Governance: An International Review," The Indian Journal of Commerce,Vol.51, No.4 , October – December 1998.
13. Tricker Robert I., International Corporate Governance, Third Edition , Prentice Hall, Singapore, 1998, pp. 465 – 70.
14. Turnbulls, S., " Corporate Governance : Theories, Challenges and Paradigms" Journal of Economic Literature, Vol.1, No.1, pp. 11 - 43.
15. http://en.wikipedia.org/wiki/Corporate_governance#Principles_of_corporate_governance
16. www.oecd.org/dataoecd/49/29/2484615.ppt
17. . [http:// www.Livemint.com](http://www.Livemint.com)
18. <http://www.sebi.gov.in>
19. www.sebi.gov.in