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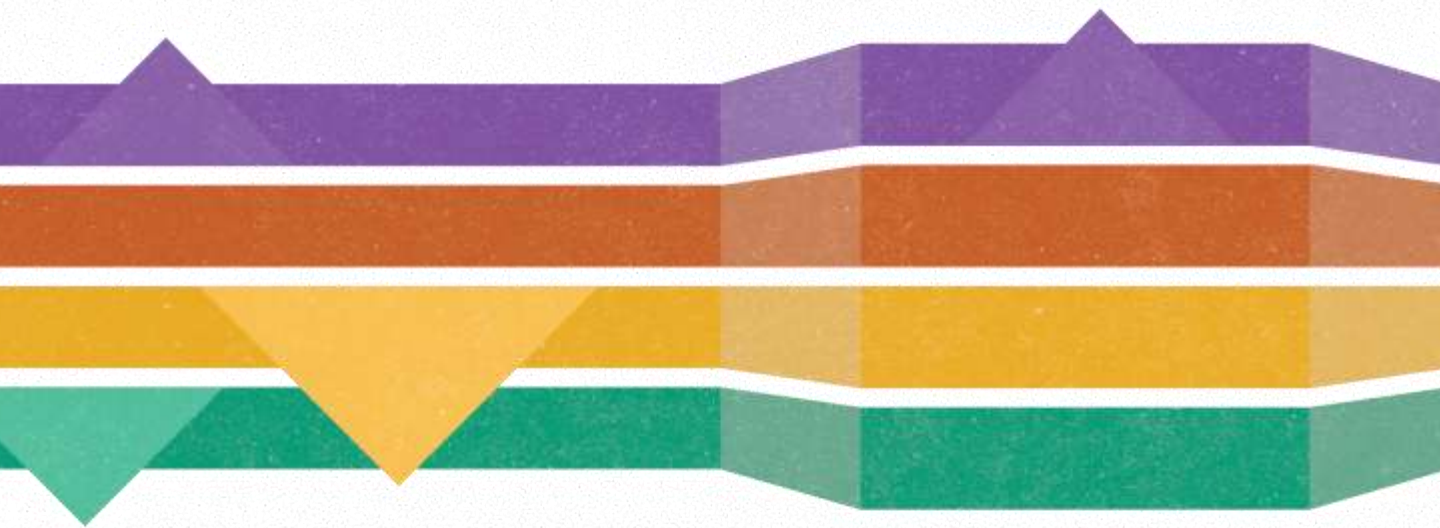
An instinct for growth™

Governance Observer

The changing face of corporate boardrooms

Volume 2

2014



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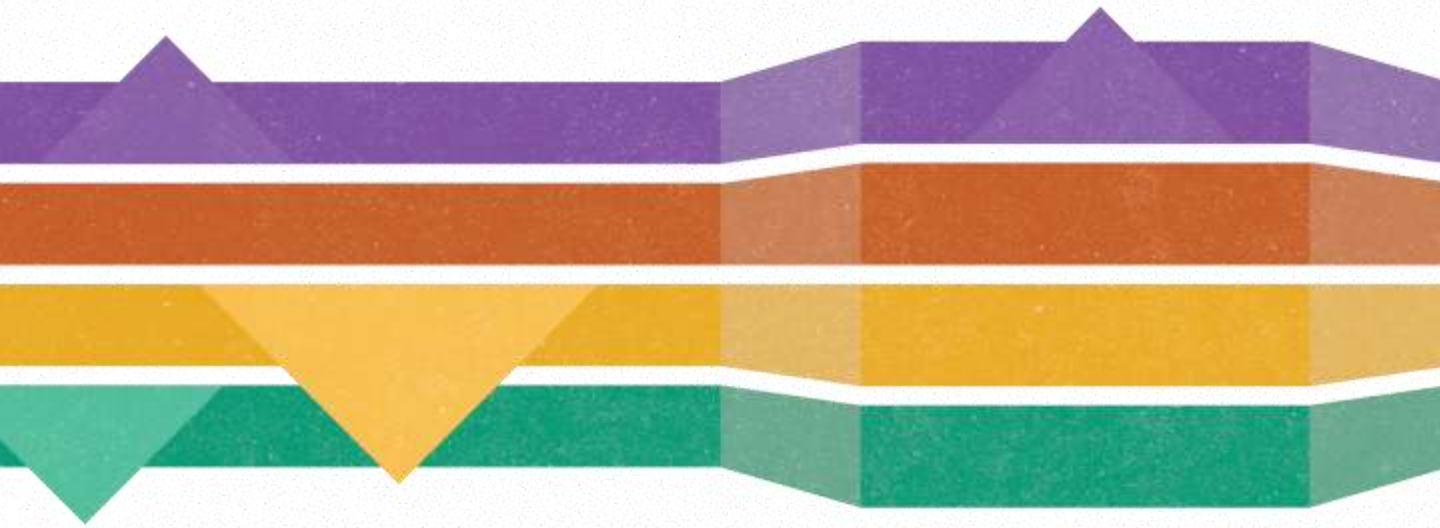
About this Publication

Governance Observer, a publication from Grant Thornton India LLP, focuses on matters relating to corporate governance. In the second edition of “**Governance Observer**”, we take a close look at the corporate Boards of India's top 150 companies by market capitalisation.

The study provides an interesting insight on Board management in India, and can serve as a benchmark for corporations to compare how their Boards are structured in relation to other companies.

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Foreword



Foreword

With stakeholder democracy seeking to manifest itself in different ways across various jurisdictions, the need has been felt more than ever before for corporates to walk the talk on governance. While the situation is not without hope, it would be useful to remember that a lot of ground is yet to be covered. Yet another development worthy of note is that over the last few years, major corporate governance failures have caused a regulatory overdrive resulting in increased compliance costs as well as in form gaining precedence over substance.

With greed increasingly informing corporate conduct, there is no need to establish the case for effective external regulation. This should not however translate to a prescriptive arrangement that is neither pragmatic, nor practical to implement. Inconsistencies between the Companies Act, 2013 ('2013 Act') and Revised Clause 49 ('RC 49') of the Listing Agreement constitute an interpretative impediment in understanding the regulatory framework that seeks to promote corporate governance. What is needed at this juncture, when India has resumed its journey on the growth path, is a set of regulations that rewards good conduct and deals with deliberate transgressions in an effective and expeditious manner.

Another feature that is worthy of mention is that the extraordinary burden placed on Independent Directors has begun to prove counterproductive, with many persons who are eminently suitable for the Board positions shying away on account of increased liability and the resultant insecurity. At the same time, there is no shortage of people seeking to join the Boards, especially of financial entities, for reasons not aligned with public interests.

The institution of Independent Directors, which is essential to strike a balance between the possible conflicts of interest among different stakeholders, has been considerably endangered by responsibilities inconsistent with their part-time role on the Board of Directors.

The auditing profession has to bear the increased burden in pursuit of the worthy cause of furthering the interest of the shareholders and other stakeholders. Related party transactions and their assessment as transactions in the ordinary course of business, and at arms length, is only one of the many onerous tasks that auditors have to perform. In the matter of dealing with frauds, where an auditor "has reason to believe that an offence involving fraud is being or has been committed", he/ she shall "immediately" report the matter to the Central Government. How this will play out, in terms of the stiff penalty for non-reporting, is unclear. With Company Secretaries being tasked in a similar fashion, the situation is not free from complications of a practical nature.



Foreword

Given all these practical considerations, the 2013 Act is in urgent need of comprehensive amendments to iron out its substantive and procedural wrinkles. At the same time, while being mindful of the shortcomings of the 2013 Act, we should not ignore the spirit behind the statutory provisions and take a technical position that does not fit well with the objective of better governance. This, more than any other, is the time when different stakeholders should work towards the common cause of raising the standards of governance in order to ensure sustainability of successful corporate entities, while not losing sight of their expectations along the sectarian lines.

History is replete with instances of major corporate failures that have destroyed not only the corporates and the interests of their stakeholders, but also dealt a body blow to the confidence levels of investors, both existing and potential. It would be worthwhile to speculate as to what might have happened had the regulatory responses been prompt and sufficiently punitive. A culture of widespread adoption of good governance practices helps in focusing on those who take liberty with stakeholders' interests, in a prompt manner.

Against this background, the task before all stakeholders is clearly cut out. The ones who draft regulations must factor in clarity, certainty and continuity, and the ones who enforce regulations must bring matters to a close quickly, effectively and in an exemplary fashion. By far, the most important requirement is for the investing class to make informed decisions, and in the process, support the corporates whose performance is premised on good governance standards. If governance remains a matter on the periphery of the radar of a corporate, an increasingly demanding stakeholder community should ensure that such corporate passes into history with considerable ignominy.

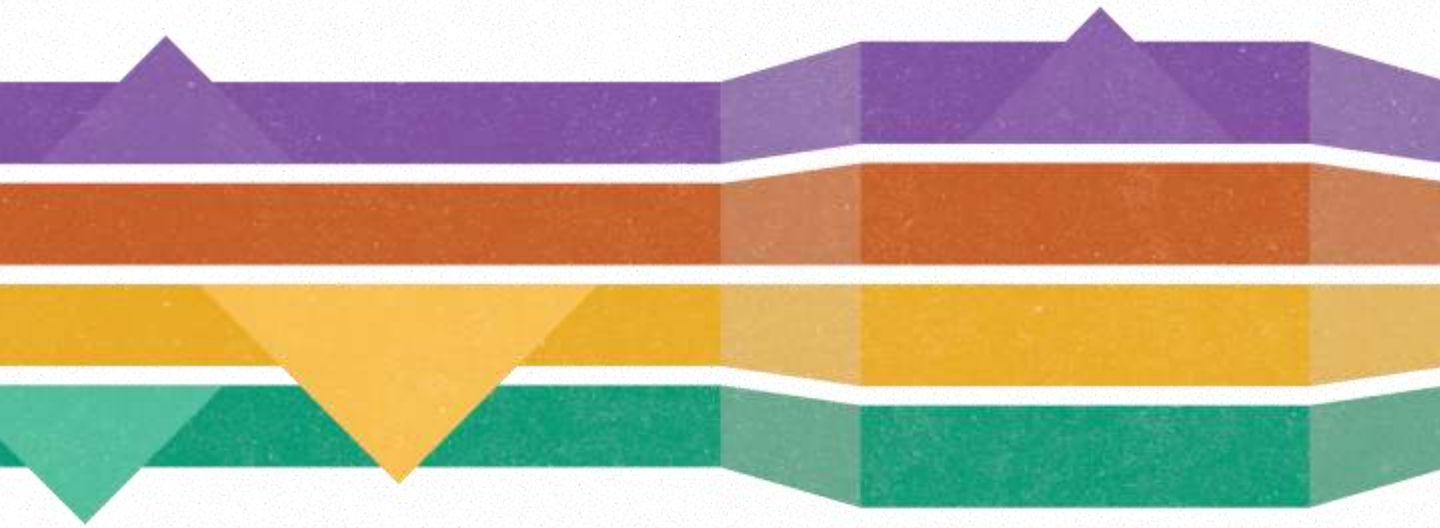
Gandhiji's twin pronouncements of businessmen being trustees and of the ends not justifying the means, should be the moral compass that guides corporates on the journey from mere compliance to sustainable performance.



M. Damodaran
Chairman,
Excellence Enablers Private
Limited and Former Chairman,
Securities and Exchange Board
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Introduction



Introduction



“Good corporate governance is about 'intellectual honesty' and not just about sticking to the rules and regulations. Capital flows towards companies that practice this type of good governance.”

- Mervyn King

The 2013 Act has further strengthened the ecosystem of governance in India and has brought with it significant additional responsibilities and duties for the Boards and corporates. It is worthwhile to remember Sir Adrian Cadbury's dictum on governance here, “corporate governance is concerned with holding the balance between economic and social goals, and between individual and communal goals. The governance framework is there to encourage the efficient use of resources and equally to ensure accountability for those resources. The aim is to align, as nearly as possible, the interests of individuals, corporations and the society.”

Corporate governance is a highly nuanced area. A cook book does not exist to guarantee compliance or to list down the benefits of good governance, but it is a must-have as the ramifications of weak governance for a corporate can be severe. History is replete with such instances and companies would ignore corporate governance at their own peril.

The 2013 Act has put down several new requirements on the corporate governance front. The chief ones include defining the tenure of independent directors, enhancing director responsibilities and disclosures on related party transactions, and providing clarity around rotation of auditors. Besides, the 2013 Act has also laid down provisions in terms of casting significant responsibility on auditors, implementation of internal controls over financial reporting framework, having woman director on the Board, whistle blower mechanism and CSR.

A general consensus exists in the corporate boardrooms that the new provisions are a good step and are welcome. But there are gaps between the principles and the prescriptions, and also lack of clarity in several areas which makes it a challenge for the companies to implement the requirement.

The 2013 Act has also been written keeping the Satyam episode in mind and hence, a number of regulations have come into being as a result of the episode. The cost of compliance is going to increase significantly and companies need to start investing in implementation. At the same time, there are plenty of areas where the desired results can be achieved by simplification, which we hope the Government will consider. As mentioned by Mervyn King, it is an attitude and cannot be achieved by addition of several rules alone.



Introduction

For example, consider the rule to have compulsory women directors. Our study shows that only 7% of the directors are women directors i.e. 1 in every 14 directorships. While this is a marginal improvement from the previous year (6%), it is evident that this provision is posing challenges in implementation for companies.

An article in the Economist (Dated: 15 November 2014) talks about the difficulties in meeting these guidelines in the Nordic countries where there is a lot of action by the state to provide women with equal opportunities (education, healthcare and generous maternity leave). We need to create other enabling support mechanisms and achieve the real benefits of having such women on the Board who can contribute. Otherwise, with typical Indian ingenuity, promoters will add a female member of the family to the Board to meet the letter but not the spirit behind the rules.

Independent directors are being asked to sign-off and take significant responsibility, which is welcome but they must be aligned to the companies' interest and benefit when the company performs. They should not be completely independent which would encourage them to act with a risk avoidance mentality that is in the long-term interest of the company.

Harish H V

Partner

Grant Thornton India LLP

About Governance Observer: Edition 2

This is the second edition of "**Governance Observer**", which is focused on providing an insight into how company Boards are structured and operate. Being the second edition, this report gives us the ability to compare how things have moved over the previous year.

The study provides several key insights, which would be useful to companies in structuring their boards and in managing them. It would also help regulators in assessing how the Board of India Inc. should look like.



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About the study



About the study

- The first edition of Governance Observer covered the annual reports and public filings for FY 2011-12 and analysed information available in the public domain on India's top 150 companies by market capitalisation
- The second edition of Governance Observer covers companies that were analysed in the first edition in light of the changes in regulatory environment and introduction of certain new aspects related to corporate governance in the 2013 Act and RC 49 of the equity listing agreements, which are effective from 01 October 2014. Key changes from the old Clause 49 ('C 49') have been highlighted in the relevant sections
- This edition also focuses on enhanced corporate governance requirements such as classification of directors, roles and responsibilities of independent directors, risk management, vigil/ whistle blower mechanism, related party transactions, codes of conduct for the Board and senior management, disclosures and remuneration of directors, Companies (Auditor's Report) Order, 2003 (CARO) reporting, etc.
- To enable easy comparison, the respective statistics from the last edition have been mentioned in brackets '['']
- The study covered a total of 1,632 active directors (existing or newly appointed directors on the Board as per the annual reports), an increase of 20 directors from the first edition [1,612 directors]
- The annual reports (FY13 - 92, FY14 - 58) and public filings of 150 companies were referred to for gathering the information
- There were 276 [247] director appointments and 173 [240] director resignations
- Information related to directors age and educational qualifications, auditor rotation, CSR, the Board's code of conduct, vigil mechanism, whistle blower policies and other disclosures were obtained from company websites and public sources
- All percentages indicate number of companies out of the total companies in respect of the sector/ region/ turnover range

About the study

The companies were classified into six sectors, four regions and five size ranges, as tabled below:

Sector	Number of companies
Banking, Financial Services and Insurance (BFSI)	30
Consumer goods	17
Healthcare & Pharma	17
Manufacturing	52
Real estate & Infrastructure (Real estate & Infra)	17
Services (Including Information Technology/ IT-enabled services)	17
Total	150

Region	Number of companies
North	35
South	27
East	9
West	79
Total	150

Turnover (INR crores)	Number of companies
< 2,500	22
2,501 - 5,000	35
5,001 -7,500	11
7,501 - 10,000	16
>10,000	66
Total	150



4

Directors and directorships



4.1 Board structure



Board structure

Number of directorships

Considering the increased responsibilities of directors, the 2013 Act mandates that a director can hold maximum directorships up to 20 companies and directorships in not more than 10 public companies.

Going forward, to enhance transparency, companies have to track and publish, in their annual reports, information about directorships held by directors in both public and private companies.

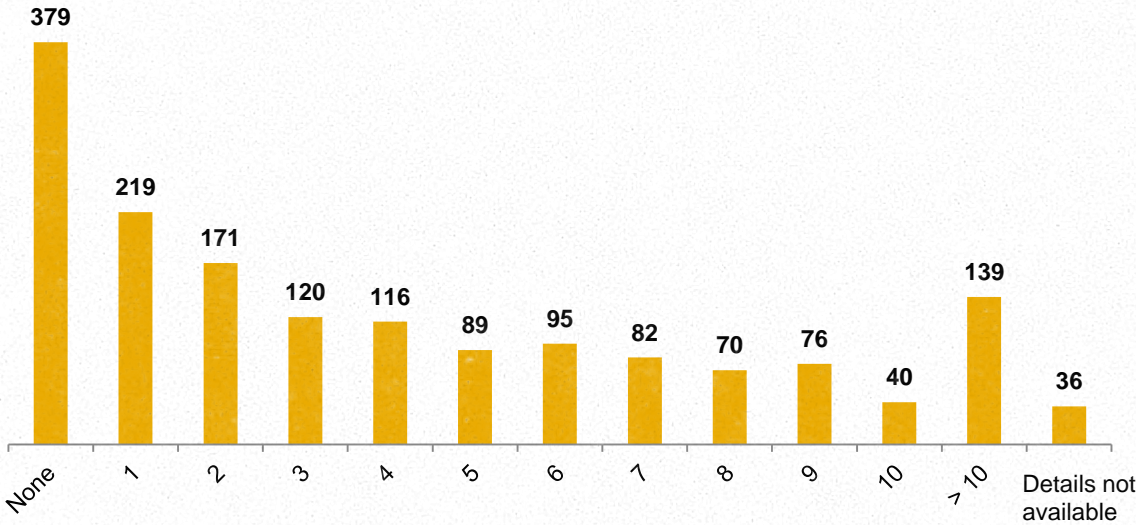
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companies provided information on the number of directorships held by directors in both public and private companies, whereas 107 companies have provided details of directorships held in public companies.

4

is the average number of directorships held by directors, a decrease of 1 directorship from 5 in the previous year.

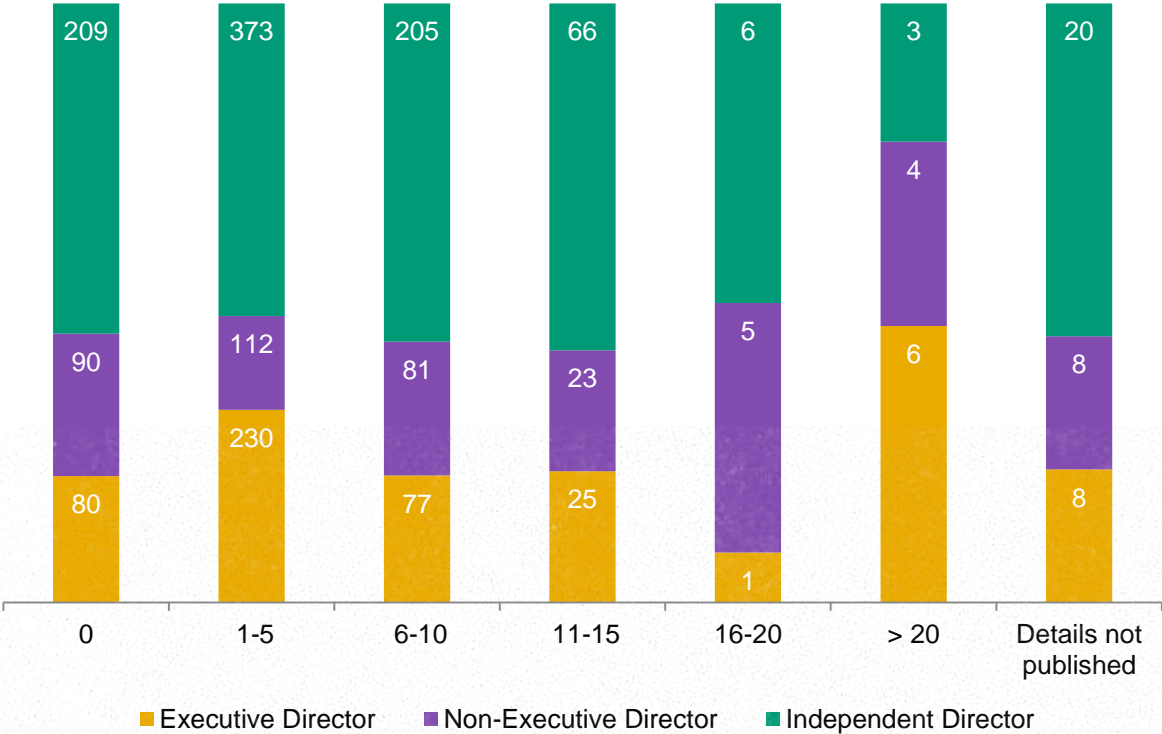
Number of additional directorships held by directors



Board structure

Number of directorships

Number of additional directorships by director type



Board structure

Code of conduct

RC 49 and the 2013 Act prescribe codes of conduct for the Board and senior management of the company. Further, RC 49 also mandates companies to host the code of conduct on their website and publish CEO's annual declaration on adherence with the code of conduct in their annual report.

85

out of 150 companies have hosted the code of conduct on the company website.

Code of conduct hosted on the company website

A. Sector-wise analysis

Number of companies: 85

% indicates percentage of companies within the sector

Figures in brackets () indicate number of companies



40%
(12)

BFSI



53%
(9)

Consumer goods



65%
(11)

Healthcare & Pharma



69%
(36)

Manufacturing



53%
(9)

Real estate & Infra



47%
(8)

Services

Board structure

Code of conduct

Code of conduct hosted on the company website

B. Region-wise analysis

Number of companies: 85

% indicates percentage of companies within the region

Figures in brackets () indicate number of companies



71%
(25)

North



51%
(40)

West



78%
(7)

East



48%
(13)

South

Board structure

Code of conduct

Code of conduct hosted on the company website

C. Company turnover-wise analysis (INR crores)

Number of companies: 85

% indicates percentage of companies within the turnover range

Figures in brackets () indicate number of companies



50%
(11)

< 2,500



57%
(20)

2,501 - 5,000



82%
(9)

5,001 - 7,500



75%
(12)

7,501 - 10,000



50%
(33)

>10,000

Board structure

Board size

Every company should be headed by an effective Board, which is collectively responsible for the long-term success of the company.

- UK Corporate Governance Code

The 2013 Act prescribes that a company shall have a maximum of 15 directors on the Board of Directors. It also states that appointing more than 15 directors would require approval of shareholders through a special resolution.

The number of directors on the Board varies between 4 and 21 [4 and 20].

Average number of directors on the Board of 150 companies is 12 [11].



Board structure

Board size

Average number of directors in a company

A. Sector-wise analysis

● 2014

● 2013



11

BFSI



10



10

Consumer goods



10



10

Healthcare and Pharma



10



12

Manufacturing



12



11

Real estate & Infra



11



11

Services



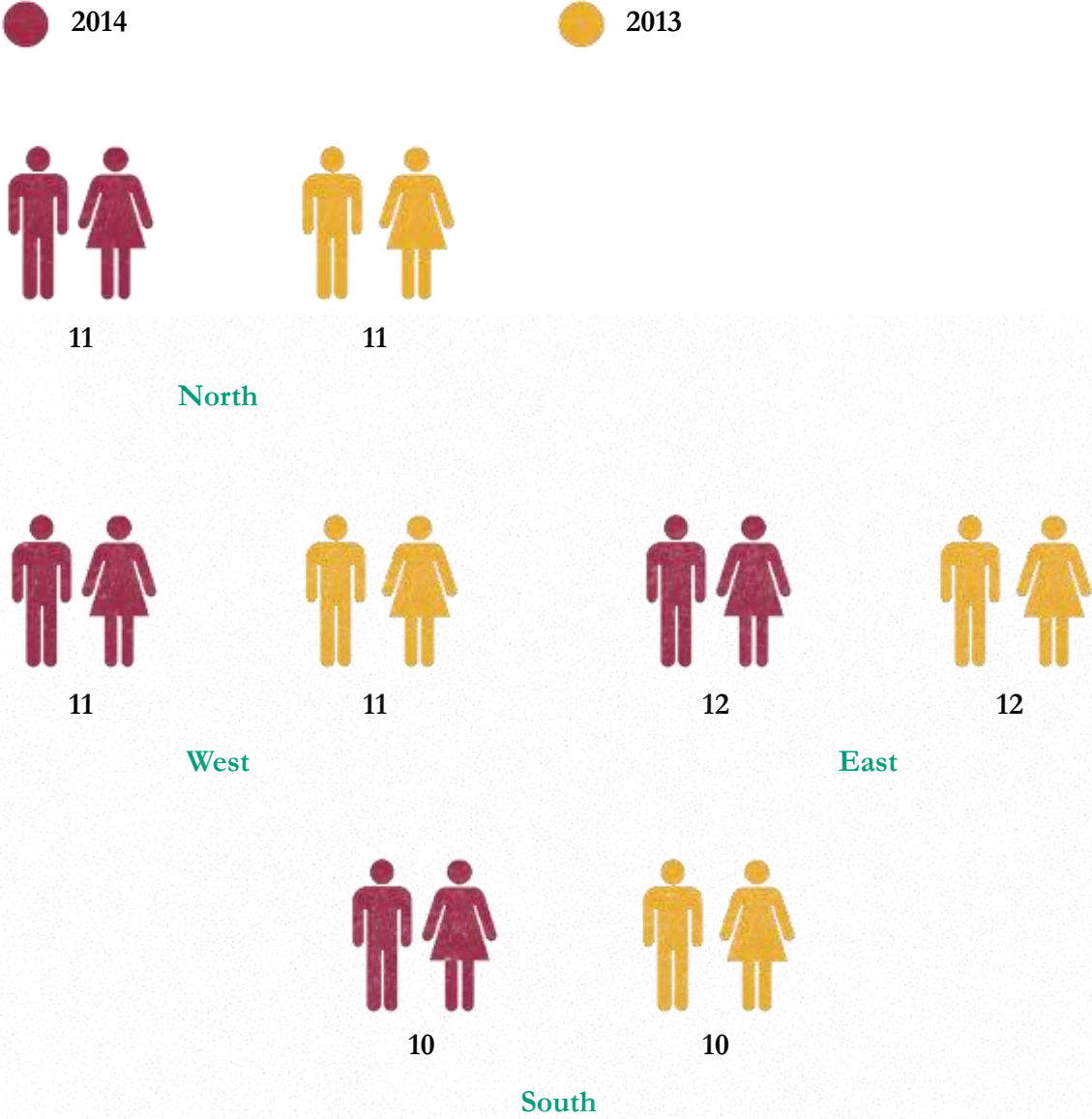
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Board structure

Board size

Average number of directors in a company

B. Region-wise analysis



Board structure

Board size

Average number of directors in a company

C. Company turnover-wise analysis (INR crores)



2014



2013



10



10

< 2,500



10



10

2,501 - 5,000



11



9

5,001 - 7,500



10



11

7,501 - 10,000



13



12

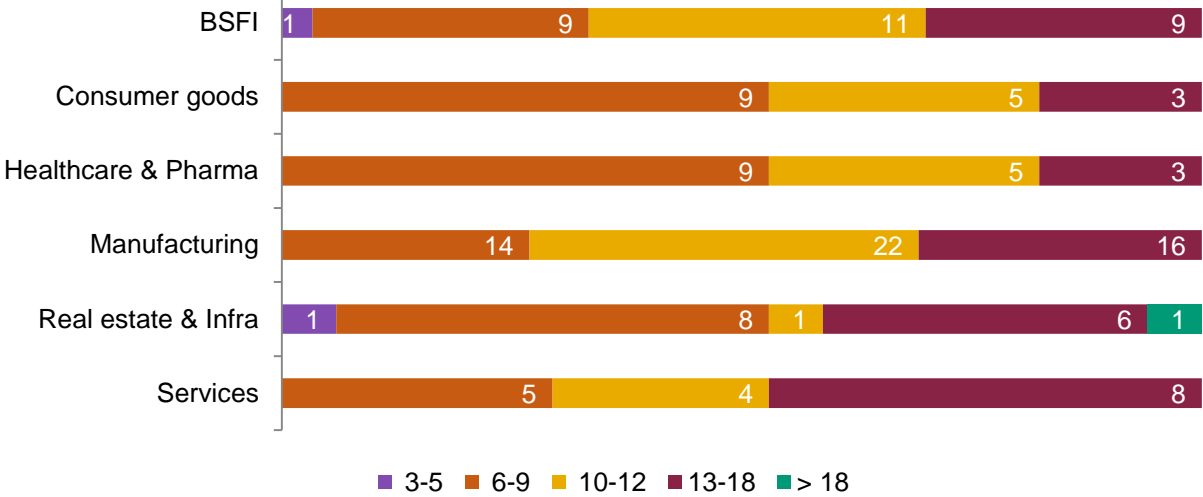
>10,000

Board structure

Board size

Number of directors in companies

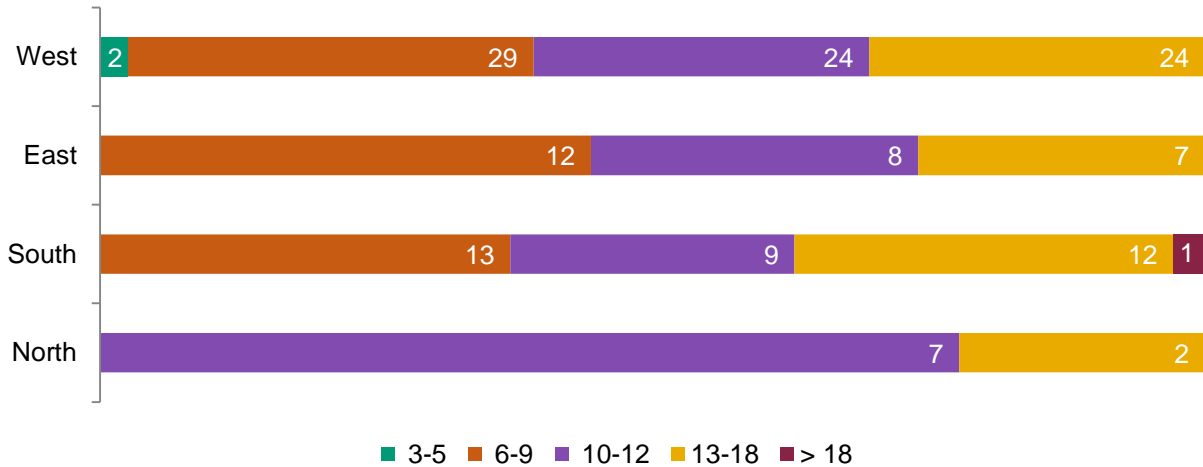
A. Sector-wise analysis



Manufacturing sector took the lead with the maximum number of directors on the Board. 22 [23] companies in this sector had 10-12 directors on their Boards, while 16 [17] companies had 13-18 directors

Number of directors in companies

B. Region-wise analysis

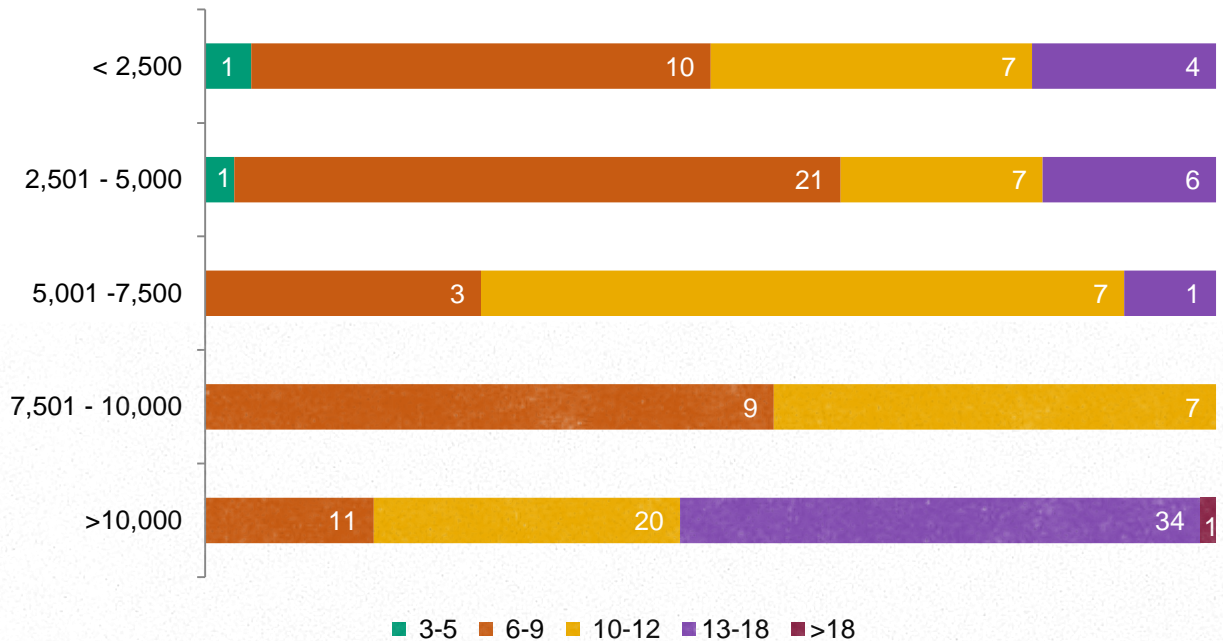


Board structure

Board size

Number of directors in companies

C. Company turnover-wise analysis (INR crores)



Companies that have turnover higher than INR 10,000 crores prefer a larger Board size. 34 [20] of these companies have 13-18 directors on their Boards, a significant increase of 14 companies when compared with the previous financial year. 20 [27] of these companies have 10-12 directors, a decrease of 7 companies year-on-year (y-o-y)

Board structure

Chairperson of the Board

The Chairperson is responsible for leading the Board and for ensuring that the Board executes its responsibilities effectively.



Segregation in the role of the Chairman and CEO

A. Sector-wise analysis

Number of companies: 102

% indicates percentage of companies within the sector

Figures in brackets () indicate number of companies



57%
(17)

BFSI



88%
(15)

Consumer goods



76%
(13)

Healthcare & Pharma



62%
(32)

Manufacturing



65%
(11)

Real estate & Infra



82%
(14)

Services

Board structure

Chairperson of the Board

Segregation in the role of the Chairman and CEO

B. Region-wise analysis

Number of companies: 102

% indicates percentage of companies within the region

Figures in brackets () indicate number of companies



49%
(17)

North



78%
(62)

West



67%
(6)

East



63%
(17)

South

Board structure

Chairperson of the Board

Segregation in the role of the Chairman and CEO

C. Company turnover-wise analysis (INR crores)

Number of companies: 102

% indicates percentage of companies within the turnover range

Figures in brackets () indicate number of companies



77%
(17)

< 2,500



69%
(24)

2,501 - 5,000



82%
(9)

5,001 -7,500



88%
(14)

7,501 - 10,000



58%
(38)

>10,000

Board structure

Chairperson of the Board

19

out of 148 companies have appointed an independent director as the Chairperson. 2 companies are yet to appoint a Chairperson.

Appointment of independent director as Chairperson

A. Sector-wise analysis

% indicates percentage of companies within the sector
Figures in brackets () indicate number of companies



17%
(8)

BFSI



6%
(8)

Consumer goods



12%
(12)

Healthcare & Pharma



13%
(23)

Manufacturing



0%
(6)

Real estate & Infra



24%
(7)

Services

Board structure

Chairperson of the Board

Appointment of independent director as Chairperson

B. Region-wise analysis

% indicates percentage of companies within the region
Figures in brackets () indicate number of companies



11%
(11)

North



15%
(39)

West



11%
(1)

East



7%
(13)

South

Board structure

Chairperson of the Board

Appointment of independent director as Chairperson

C. Company turnover-wise analysis (INR crores)

% indicates percentage of companies within the turnover range
Figures in brackets () indicate number of companies



14%
(13)

< 2,500



14%
(12)

2,501 - 5,000



27%
(11)

5,001 - 7,500



13%
(4)

7,501 - 10,000



9%
(24)

>10,000

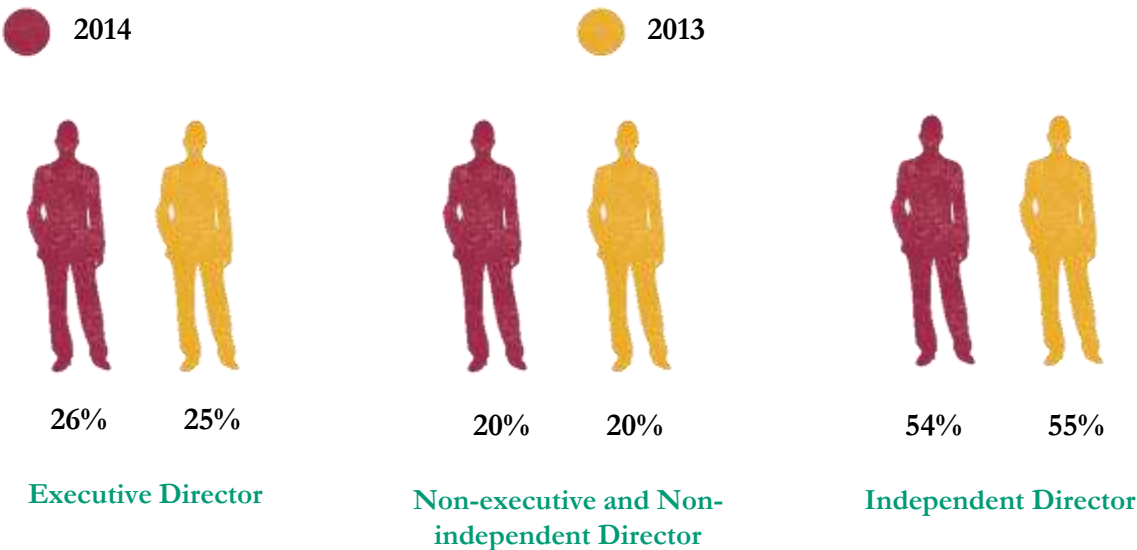
Board structure

Executive and Non-executive directors

"As members of a unitary Board, Non-executive directors should constructively challenge and help develop proposals on strategy."

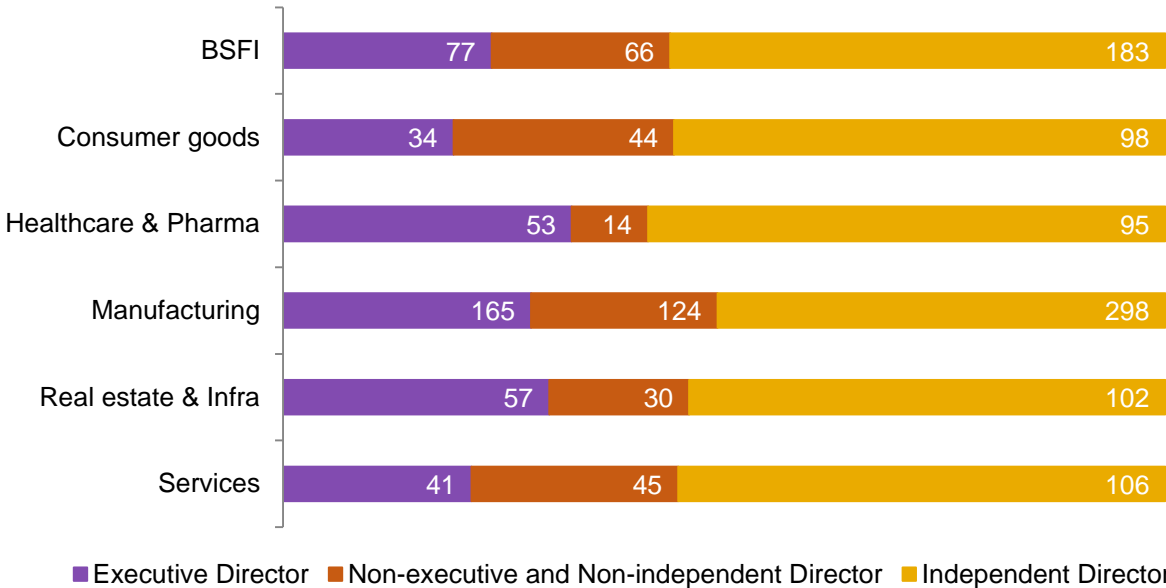
- UK Corporate Governance Code

Directors by type



Composition of directors

A. Sector-wise analysis

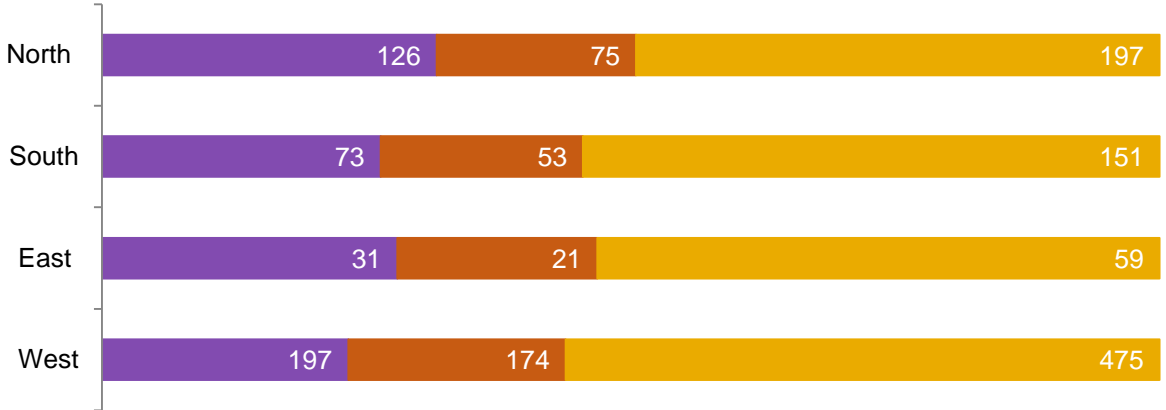


Board structure

Executive and Non-executive directors

Composition of directors

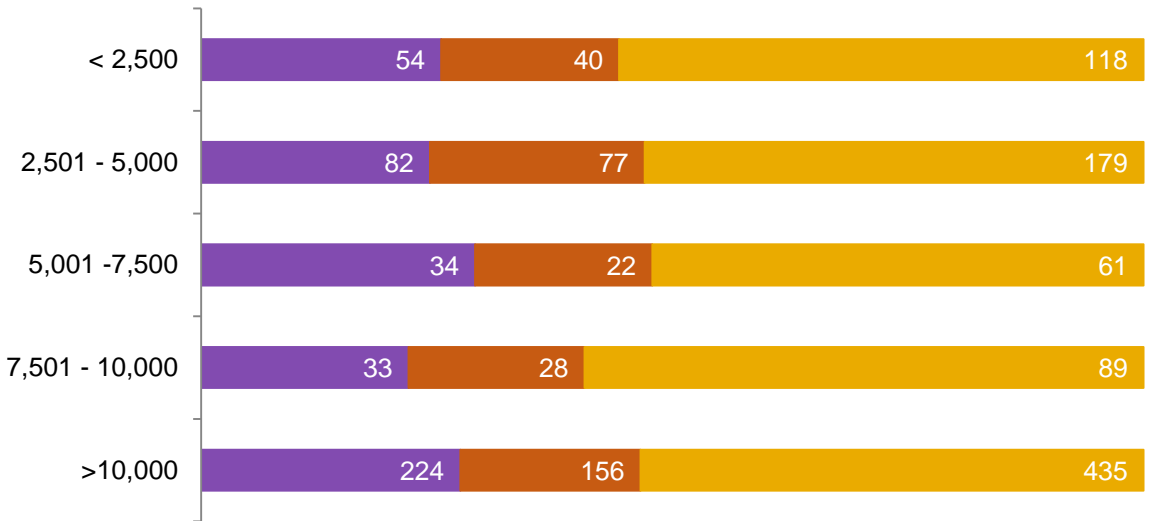
B. Region-wise analysis



■ Executive Director ■ Non-executive and Non-independent Director ■ Independent Director

Composition of directors

C. Company turnover-wise analysis (INR crores)



■ Executive Director ■ Non-executive and Non-independent Director ■ Independent Director

Board structure

Audit Committee composition

As per the 2013 Act, an Audit Committee comprises minimum of three directors, with independent directors being the majority.

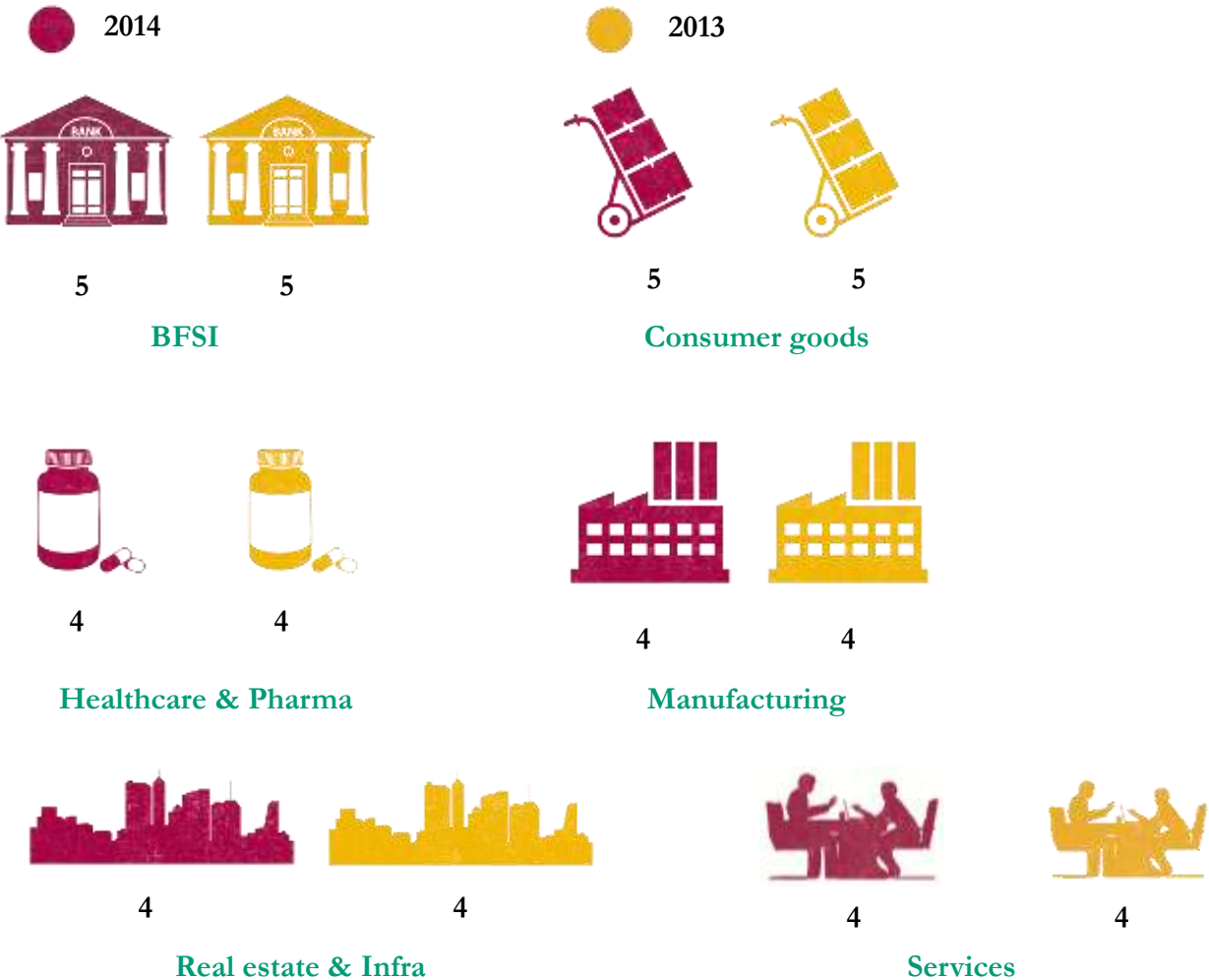
As per RC 49, the Audit Committee should comprise minimum of three directors, with two-third members being independent directors.

Roles and activities of the Audit Committee have been specifically provided under the 2013 Act and RC 49.

529 out of 666 (79%) directors on the Audit Committees of 150 listed companies are independent directors. [522 out of 636 - 82%].

Comparison of the average size of Audit Committee

A. Sector-wise analysis



Board structure

Audit Committee composition

64 out of 150 listed companies have only independent directors on the Audit Committees.

Companies that have only independent directors on the Audit Committee

A. Sector-wise analysis

Number of companies: 64

% indicates percentage of companies within the sector

Figures in brackets () indicate number of companies



27%
(8)

BFSI



47%
(8)

Consumer goods



71%
(12)

Healthcare & Pharma



44%
(23)

Manufacturing



35%
(6)

Real estate & Infra



41%
(7)

Services

Comparison of the average size of Audit Committee

B. Region-wise analysis

Number of companies: 64

% indicates percentage of companies within the region

Figures in brackets () indicate number of companies



31%
(11)

North



48%
(13)

South



11%
(1)

East



49%
(39)

West

Board structure

Audit Committee composition

Comparison of the average size of Audit Committee

C. Company turnover-wise analysis (INR crores)

Number of companies: 64

% indicates percentage of companies within the turnover range

Figures in brackets () indicate number of companies



59%
(13)

< 2,500



34%
(12)

2,501 - 5,000



100%
(11)

5,001 - 7,500



25%
(4)

7,501 - 10,000



36%
(24)

>10,000



All companies (11 companies) with turnover ranging from INR 5,001 crores to INR 7,500 crores have only independent directors as Audit Committee members

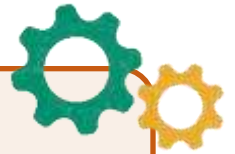
141

companies (94%) [93%] of 150 listed companies have an independent director as the Audit Committee Chairperson.

Board structure

Resident Director

The 2013 Act mandates a company to have at least one director who has stayed in India for a total period of not less than 182 days in the previous calendar year, which should be consistent with the calendar year followed for deduction of income tax.



Companies have to develop a mechanism to track directors' stay outside India.



Board structure

Remuneration of Directors

RC 49 and the 2013 Act mandate the constitution of a Board-level committee to look into the nomination and remuneration of directors.

74 out of 150 companies reported the presence of a Nomination Committee. For these companies, Board succession planning was a primary objective.



Board structure

Nomination Committee

Companies that have a Nomination Committee

A. Sector-wise analysis

Number of companies: 74
% indicates percentage of companies within the sector
Figures in brackets () indicate number of companies



77%
(23)

BFSI



47%
(8)

Consumer goods



47%
(8)

Healthcare & Pharma



38%
(20)

Manufacturing



35%
(6)

Real estate & Infra



53%
(9)

Services

Board structure

Nomination Committee

Companies that have a Nomination Committee

B. Region-wise analysis

Number of companies: 74
% indicates percentage of companies within the region
Figures in brackets () indicate number of companies



43%
(15)

North



56%
(5)

East



49%
(39)

West



56%
(15)

South

Board structure

Nomination Committee

Companies that have a Nomination Committee

C. Company turnover-wise analysis (INR crores)

Number of companies: 74
% indicates percentage of companies within the turnover range
Figures in brackets () indicate number of companies



36%
(8)

< 2,500



40%
(14)

2,501 - 5,000



55%
(6)

5,001 - 7,500



63%
(10)

7,501 - 10,000



55%
(36)

> 10,000

Board structure

Remuneration Committee

133 out of 150 companies reported that they have a committee to review directors' remuneration.

Companies that have a Remuneration Committee

A. Sector-wise analysis

Number of companies: 133

% indicates percentage of companies within the sector

Figures in brackets () indicate number of companies



93%
(28)

BFSI



94%
(16)

Consumer goods



82%
(14)

Healthcare & Pharma



83%
(43)

Manufacturing



94%
(16)

Real estate & Infra



94%
(16)

Services

Board structure

Remuneration Committee

Companies that have a Remuneration Committee

B. Region-wise analysis

Number of companies: 133

% indicates percentage of companies within the region

Figures in brackets () indicate number of companies



86%
(30)

North



86%
(68)

West



100%
(9)

East



96%
(26)

South

Board structure

Remuneration Committee

Companies that have a Remuneration Committee

C. Company turnover-wise analysis (INR crores)

Number of companies: 133

% indicates percentage of companies within the turnover range

Figures in brackets () indicate number of companies



91%
(20)

< 2,500



89%
(31)

2,501 - 5,000



91%
(10)

5,001 - 7,500



81%
(13)

7,501 - 10,000



89%
(59)

>10,000



Board structure

Remuneration Committee

Both the 2013 Act and RC 49 mandate the Remuneration Committee to comprise three or more non-executive directors. Further, majority should be independent directors.

123

out of the 133 companies, mentioned above, have three or more non-executive directors as members of the Remuneration Committee.

114

out of 123 companies that have a Remuneration Committee, majority of the members are independent directors. Of the 114 companies, 56 companies have a Remuneration Committee with only independent directors as its members.



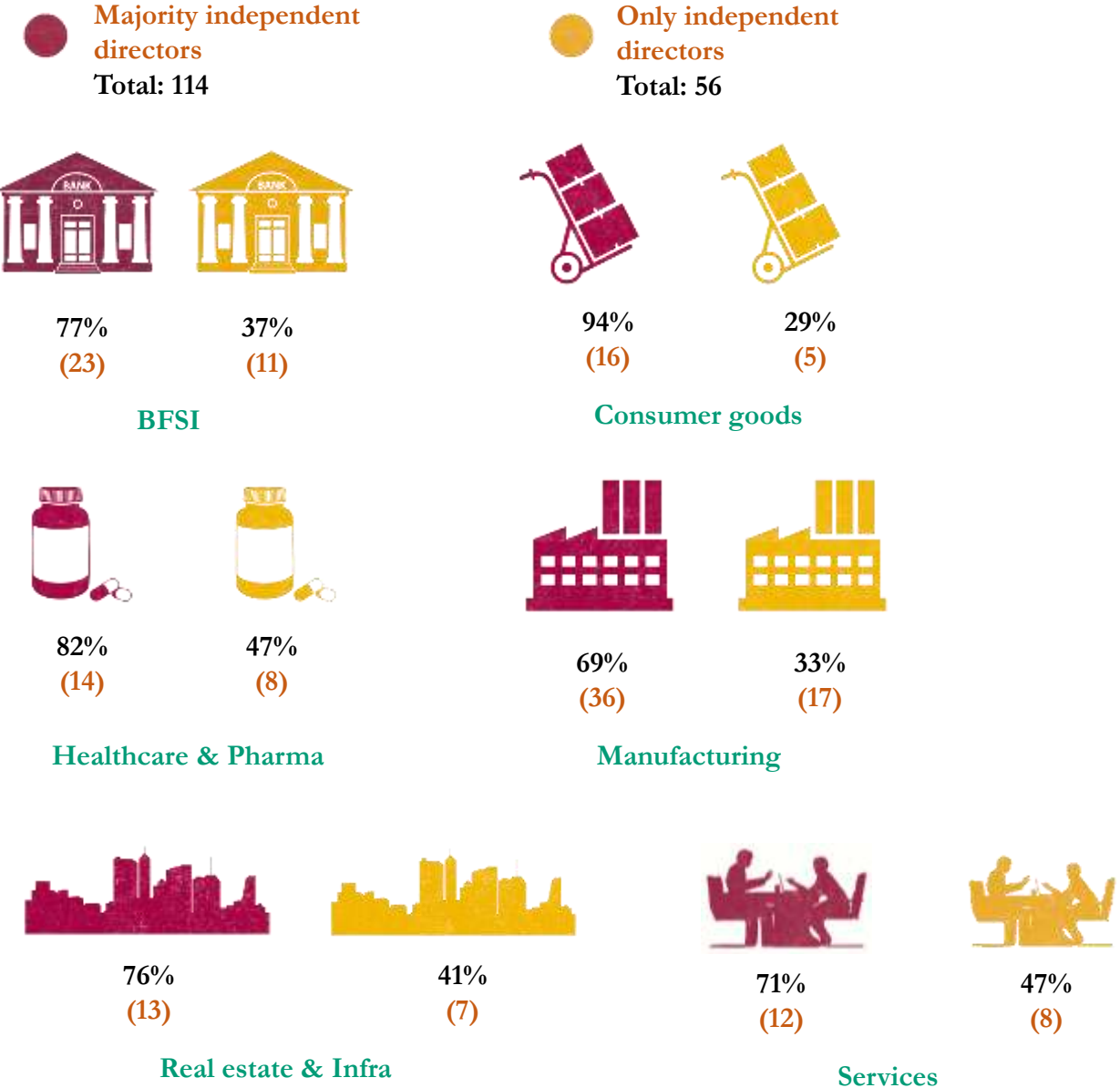
Board structure

Remuneration Committee

Companies with majority and only independent directors in the Remuneration Committee

A. Sector-wise analysis

% indicates percentage of companies within the sector
 Figures in brackets () indicate number of companies



Note: 56 companies are a subset of 114 companies

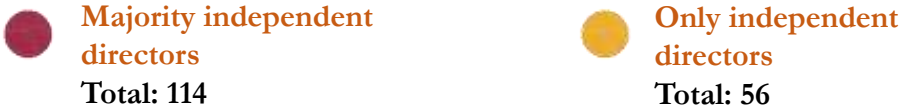
Board structure

Remuneration Committee

Companies with majority and only independent directors in the Remuneration Committee

B. Region-wise analysis

% indicates percentage of companies within the region
 Figures in brackets () indicate number of companies



80%
(28)



34%
(12)

North



67%
(53)



33%
(26)



100%
(9)



33%
(3)

West

East



89%
(24)



56%
(15)

South

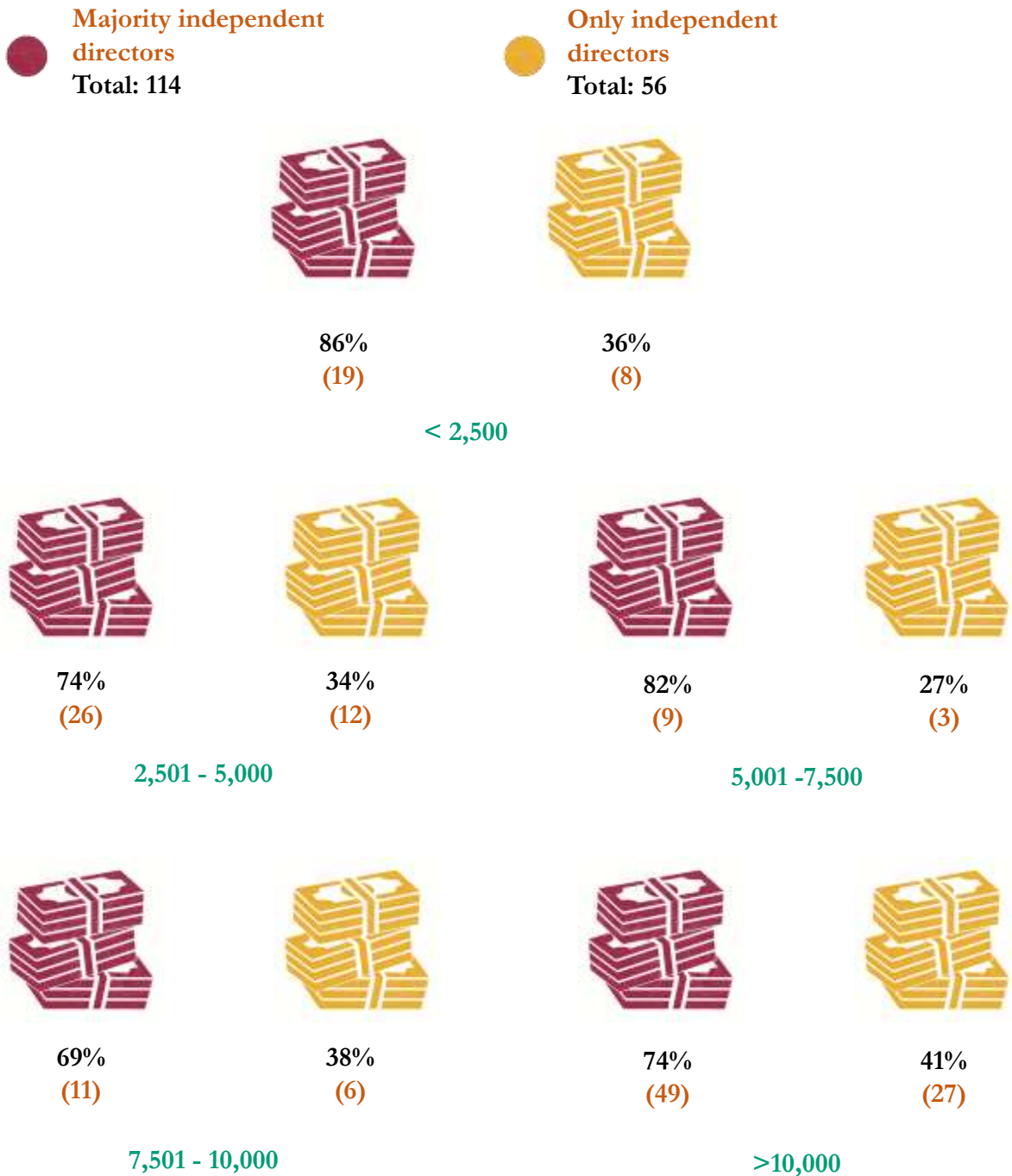
Board structure

Remuneration Committee

Companies with majority and only independent directors in the Remuneration Committee

C. Company turnover-wise analysis (INR crores)

% indicates percentage of companies within the turnover range
 Figures in brackets () indicate number of companies



Board structure

Remuneration Committee

RC 49 prescribes that the Chairperson of the Remuneration Committee should be an independent director. However, the Chairperson of the company cannot be the Chairperson of the Remuneration Committee.

10

out of 150 companies, are such wherein Chairperson of the company is also the Chairperson of the Remuneration Committee.

106

out of 123 companies are such wherein an independent director is the Chairperson of the Remuneration Committee.

Companies that have independent director as the Chairperson of the Remuneration Committee

A. Sector-wise analysis

Number of companies: 106

% indicates percentage of companies within the sector

Figures in brackets () indicate number of companies



53%
(16)

BFSI



88%
(15)

Consumer goods



76%
(13)

Healthcare & Pharma



73%
(38)

Manufacturing



71%
(12)

Real estate & Infra



71%
(12)

Services

Board structure

Remuneration Committee

Companies that have independent director as the Chairperson of the Remuneration Committee

B. Region-wise analysis

Number of companies: 106

% indicates percentage of companies within the region

Figures in brackets () indicate number of companies



86%
(24)

North



86%
(53)

West



100%
(8)

East



96%
(21)

South

Board structure

Remuneration Committee

Companies that have independent director as the Chairperson of the Remuneration Committee

C. Company turnover-wise analysis (INR crores)

Number of companies: 106

% indicates percentage of companies within the turnover range

Figures in brackets () indicate number of companies



82%
(18)

< 2,500



71%
(25)

2,501 - 5,000



64%
(7)

5,001 -7,500



69%
(11)

7,501 - 10,000



68%
(45)

>10,000

Expert view



Corporate governance or more correctly "good corporate governance(GCG)" has become a near universal mantra which is fast developing into a cliché. It provides a cornucopia of riches for consultants, lawyers and others who thrive on the seminar circuit. I shall not add to that crowd in this short piece.

GCG is a self-evident requirement when an enterprise requires funds from any third party - be it equity or loans. The outsider wants to be reassured that his money is safe. Also, other stakeholders such as employees, governments, suppliers and customers all would want to make sure that their needs are properly addressed.

Why then does GCG continue to elude many? Previously, the reason used to be lack of knowledge/ understanding, but with the plethora of information now provided that defence is not sustainable, so it must be more than that. It is, I believe, a combination of some lack of understanding but also disregard for the rigour of GCG. So, until the fundamental mindsets are not changed, GCG will largely be paying of lip service to the latest trend. How can this attitude be changed? Can it ever be changed? These are difficult questions to answer. Maybe after India becomes a physically clean nation, we can hope to clear the path to GCG!



E A Kshirsagar
Leading Independent Director

4.2 Directors' credentials



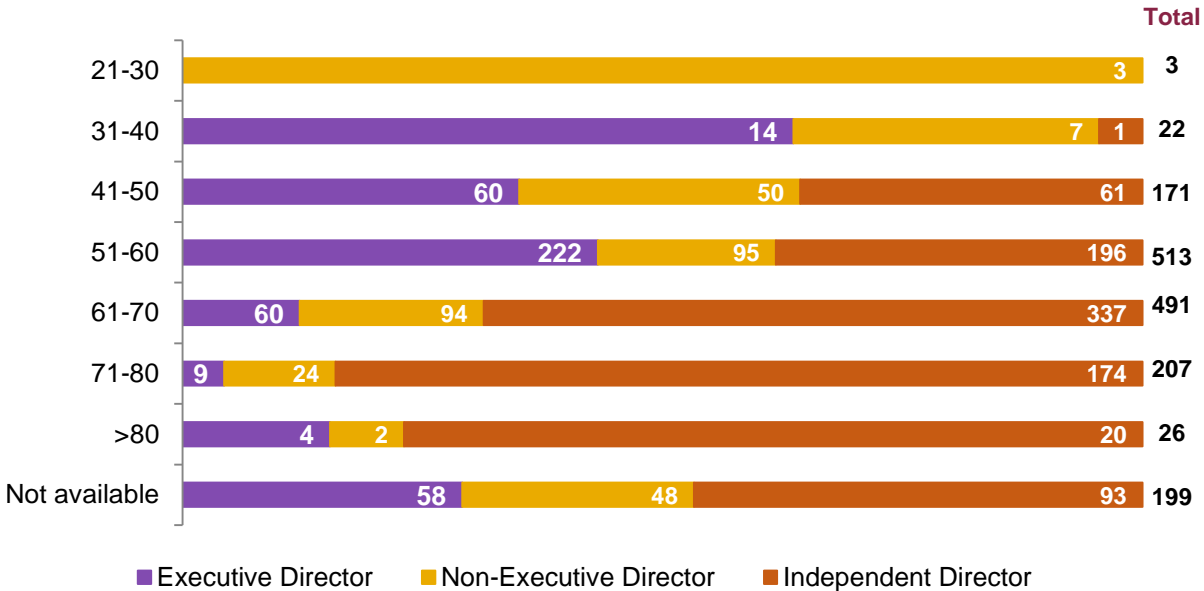
Directors' credentials

Age of directors

Age of the directors was compiled from annual reports and the public domain. The following table provides year-on-year (y-o-y) comparison of the data available for the age of directors.

Year	Number of directors		Total
	Data available	Data not available	
2014	1433	199	1632
2013	1453	159	1612

Type of director and age range



26 directors (2%) are more than 80 years old, [29 directors; 2%]



724 directors (44%) are aged more than 60 years [711 directors; 49%]



65 years is the average age of independent directors

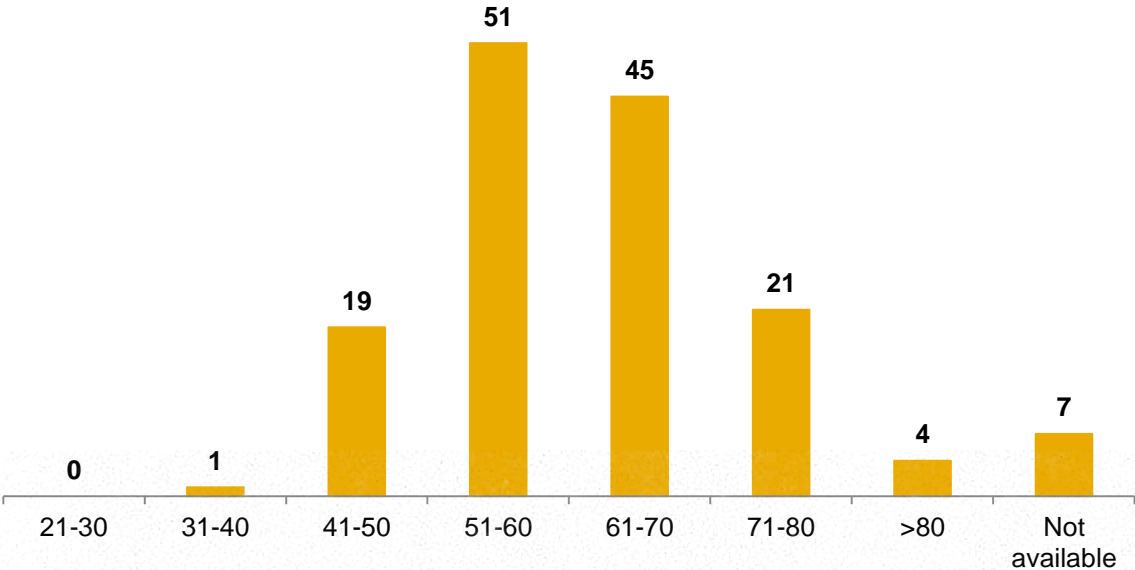


60% of independent directors [65%] are more than 60 years old

Directors' credentials

Age of directors

Age range of Chairpersons



Directors' credentials

Educational qualifications

The 2013 Act mandates majority of Audit Committee members, including its Chairperson, to be proficient at reading and understanding the financial statements. However, RC 49 prescribes that all members should be financially literate, and at least one member should have accounting or related financial management expertise.



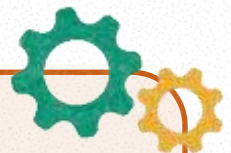
Information related to educational qualification was not available for 114 directors [96 directors] out of 1632 directors



420 out of 1518 directors are graduates or have a lower than bachelor's degree [424 out of 1513]



1098 [1030] directors have a professional degree



The Board and its committees should have the skills, experience and independence, and knowledge of the company in order to carry out their duties and responsibilities effectively.

- UK Corporate Governance Code

Expert view



One of the rampant ways of complying with the corporate governance guidelines is by employing consultants - the common refrain being 'we won't do it but let us get someone else to do it for us'. Basically, we hire consultants not to advise us but more to act as facilitators and expedite matters for us. I have been told that this is legally acceptable and is practiced quite widely. But is it ethically correct? In my opinion, No!

The question is not to distance ourselves from anything disreputable but to discontinue it altogether. To answer the question - whether consultants can serve as facilitators, a disclosure needs to be incorporated within some acceptable guidelines - either on the sum involved or the period of appointment or through some other approval mechanism.



Naresh Malhotra

CEO, Modern Family Doctor

Also serves as an Independent Director for several companies

4.3 Women directors



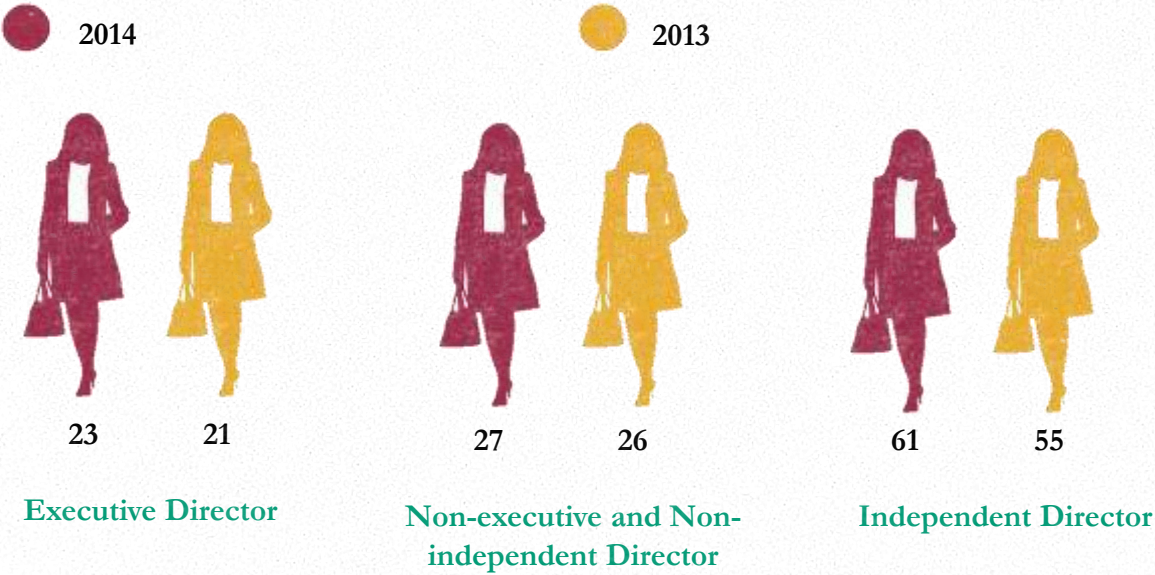
Women directors

RC 49 prescribes a minimum of one woman director on the Board of listed companies. Besides, the 2013 Act prescribes a minimum of one woman director on the Board for certain classes of companies.

1 in every 14 directorships is held by a woman, a positive increase compared to 2013 where 1 in every 17 directorships was held by a woman.

111 out of 1632 (7%) directors are women.

Type of women directors

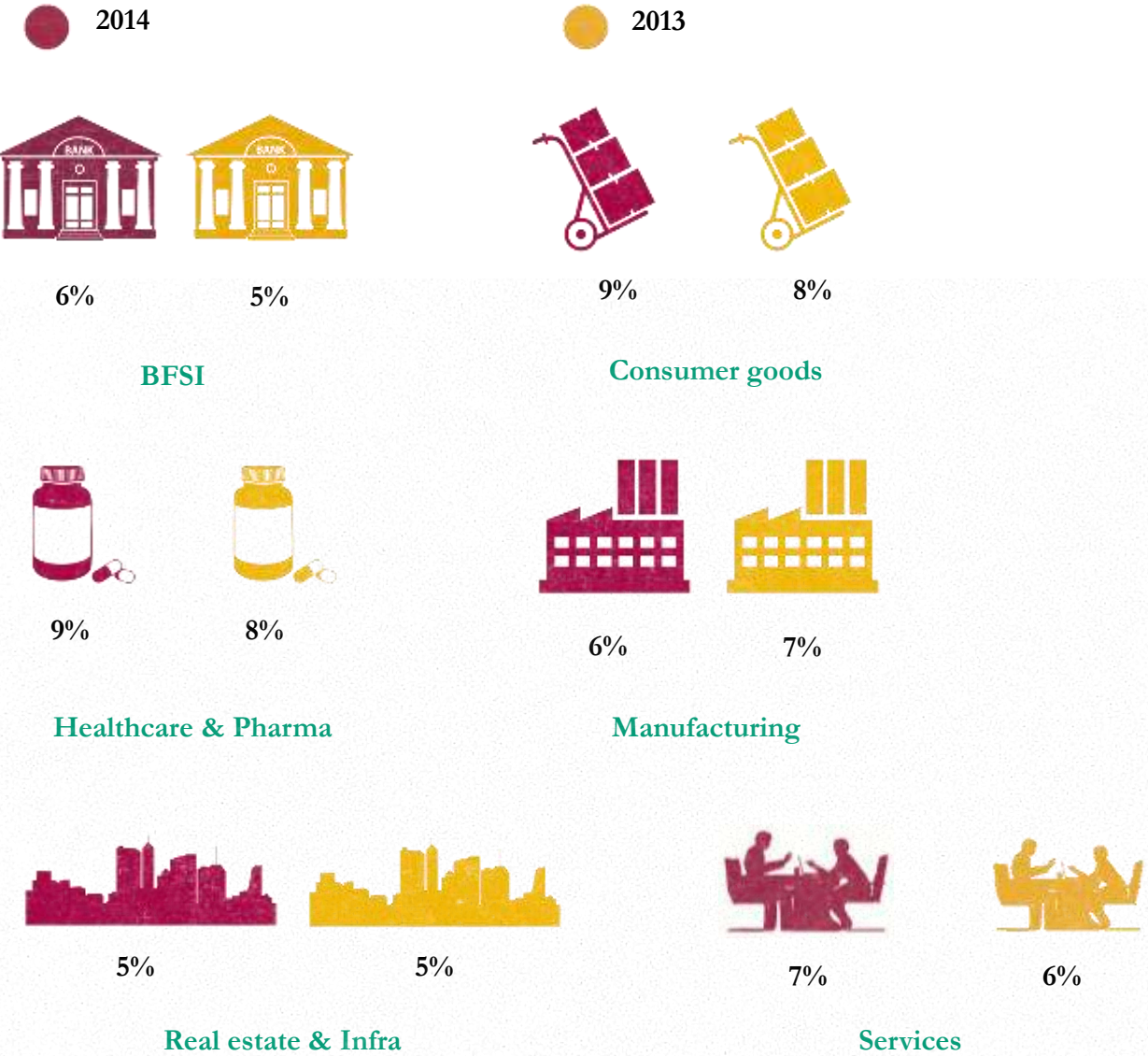


Women directors

Women representation on the Board

A. Sector-wise analysis

% indicates percentage of companies within the sector

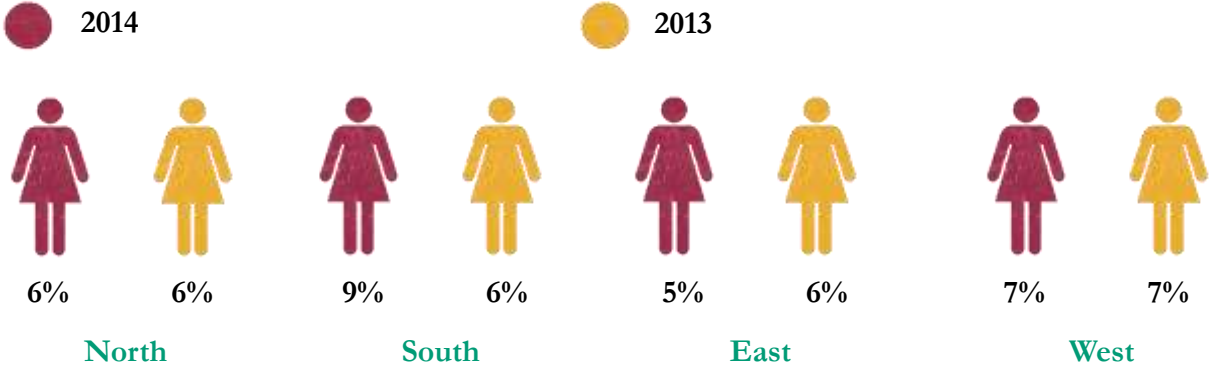


Women directors

Women representation on the Board

B. Region-wise analysis

% indicates percentage of companies within the region



Women representation on the Board

C. Company turnover-wise analysis (INR crores)

% indicates percentage of companies within the turnover range

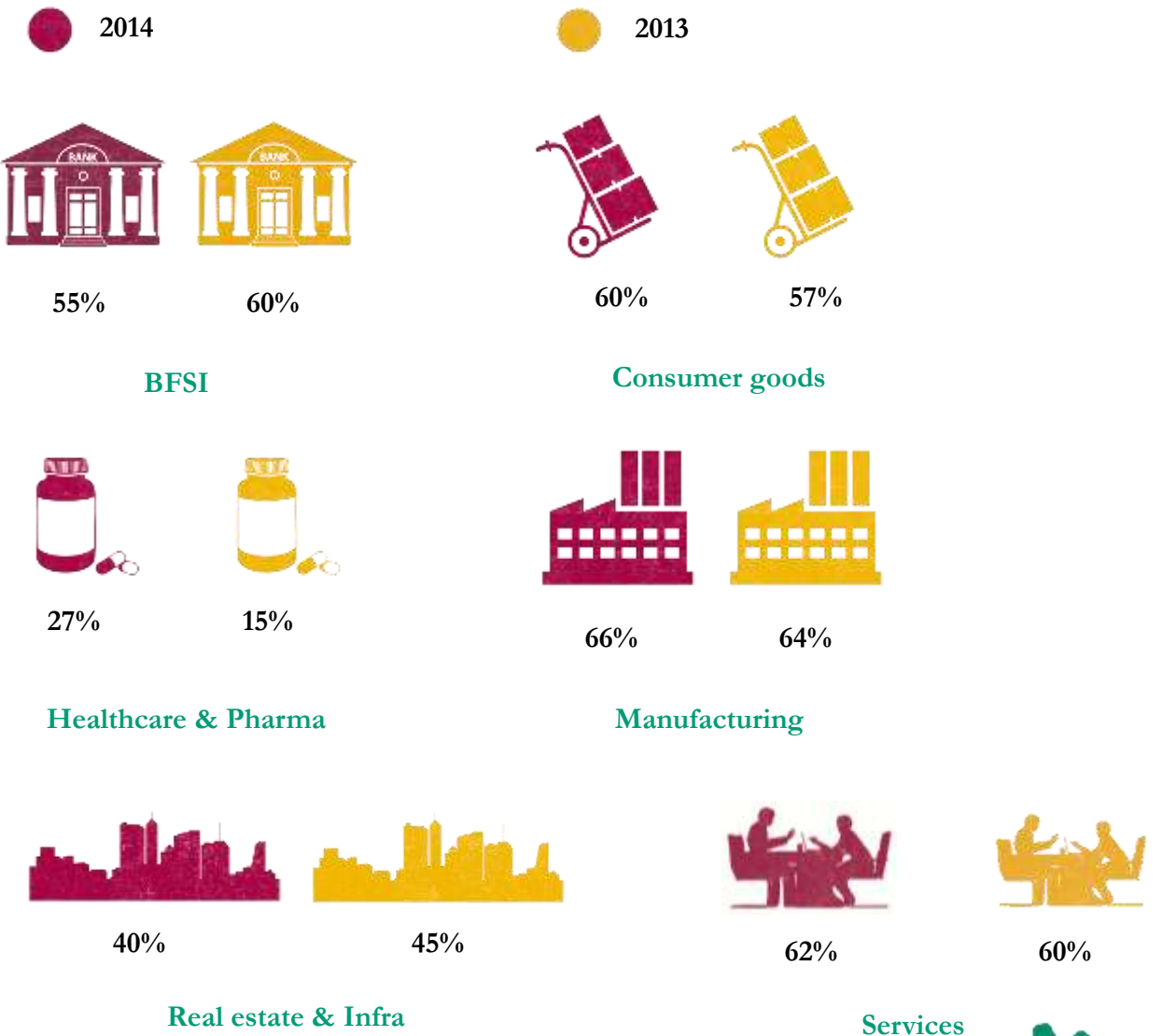


Women directors

Independent women directors out of the total women directors on the Board

A. Sector-wise analysis

% indicates percentage of companies within the sector



In consideration of the challenges faced by companies in conforming with the women directorship provision, SEBI has extended the date of compliance to 1 April 2015.

Women directors

Independent women directors out of the total women directors on the Board

B. Region-wise analysis

% indicates percentage of companies within the sector



2014



2013



59%

57%

North



49%

49%

West



50%

57%

East



67%

65%

South

Women directors

Independent women directors out of the total women directors on the Board

C. Company turnover-wise analysis

% indicates percentage of companies within the sector



2014



2013



44%



42%

< 2,500



38%



25%

2,501 - 5,000



50%



58%

5,001 - 7,500



79%



69%

7,501 - 10,000



59%



64%

Expert view



The 2013 Act focuses on corporate governance, beyond the financials. Board oversight, which is mandated on the aspect of human capital framework for senior management, key management personnel and board members is a welcome step. The requirement of defining key attributes of leaders and board members, involvement in their selection, performance evaluation, succession planning and remuneration widens the charter of the Board's nominations and that of the Remuneration Committees beyond those prescribed for erstwhile Compensation Committees.

Of course progressive Boards have embraced many of the outlined practices proactively even before the 2013 Act came into play. For others, these guidelines will provide a good framework for holistic governance at the Board level. While putting these into practice, it is important that the Board and the Executive Management teams articulate their respective roles clearly, remembering that the expectation from the Board is to provide oversight. Boards are not expected to venture into the executive realm.



Hema Ravichandar
Strategic HR Advisor and
Member of the Board,
Marico Limited and Titan
Company Limited

4.4 Meetings and attendance



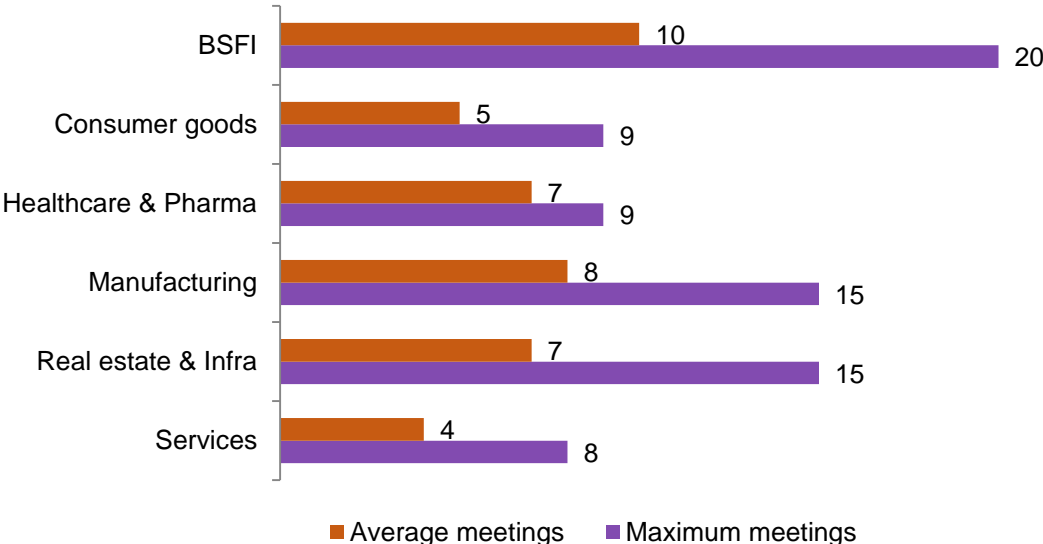
Meetings and attendance

Board meetings and attendance

The average number of Board meetings was 7, with a range of 4 to 20 meetings [average 7; range 4 to 20 meetings].

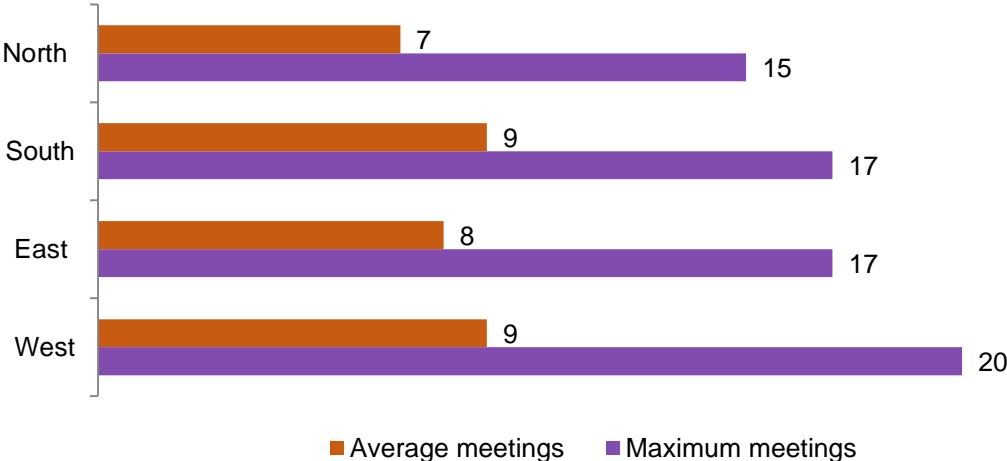
Maximum and average number of Board meetings

A. Sector-wise analysis



Maximum and average number of Board meetings

B. Region-wise analysis

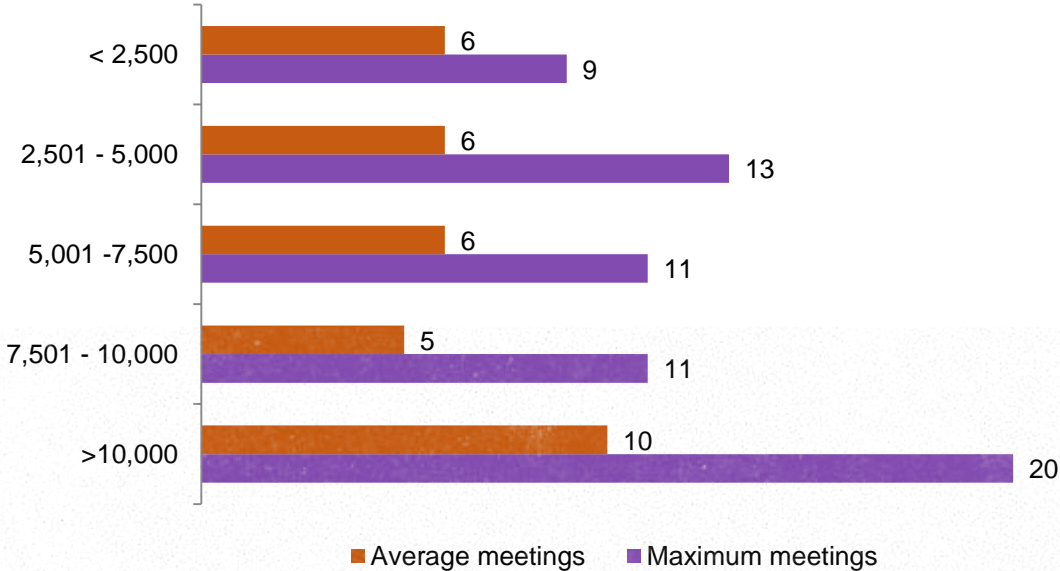


Meetings and attendance

Board meetings and attendance

Maximum and average number of Board meetings

C. Company turnover-wise analysis (INR crores)



Average attendance of directors in Board meetings was found to be 83% [85%]

Meetings and attendance

Board meetings and attendance

Average attendance of Executive Directors, Non-executive and Non-independent Directors, and Independent Directors



158 directors of such companies that held more than four meetings, attended less than four Board meetings [251 directors; 16%].

Meetings and attendance

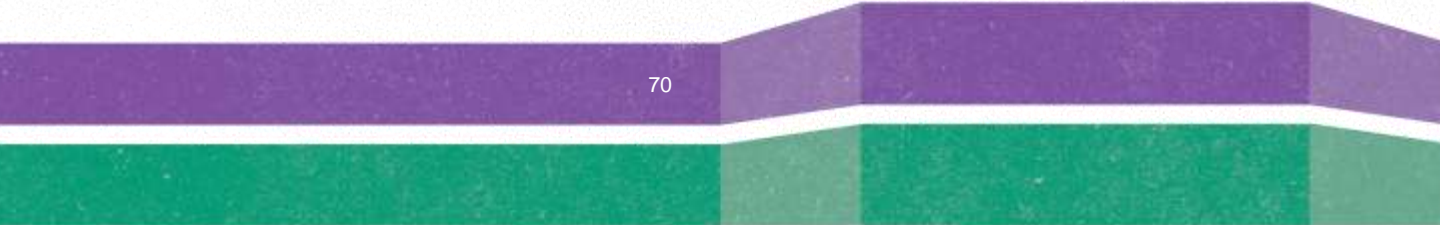
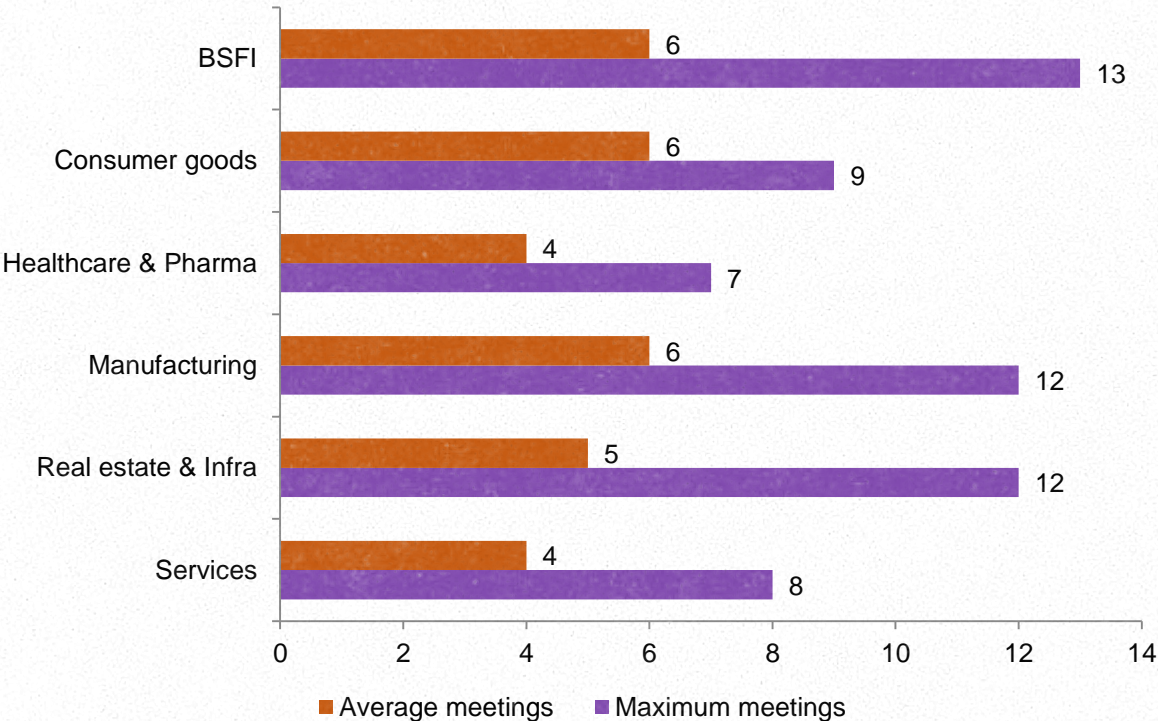
Audit Committee meetings and attendance

140 companies have conducted more than the prescribed minimum of four meetings in a year.

Number of Audit Committee meetings varied from 4 to 13 [4 to 15 meetings] and the average number of meetings was 6 [6].

Maximum and average number of Audit Committee meetings

A. Sector-wise analysis

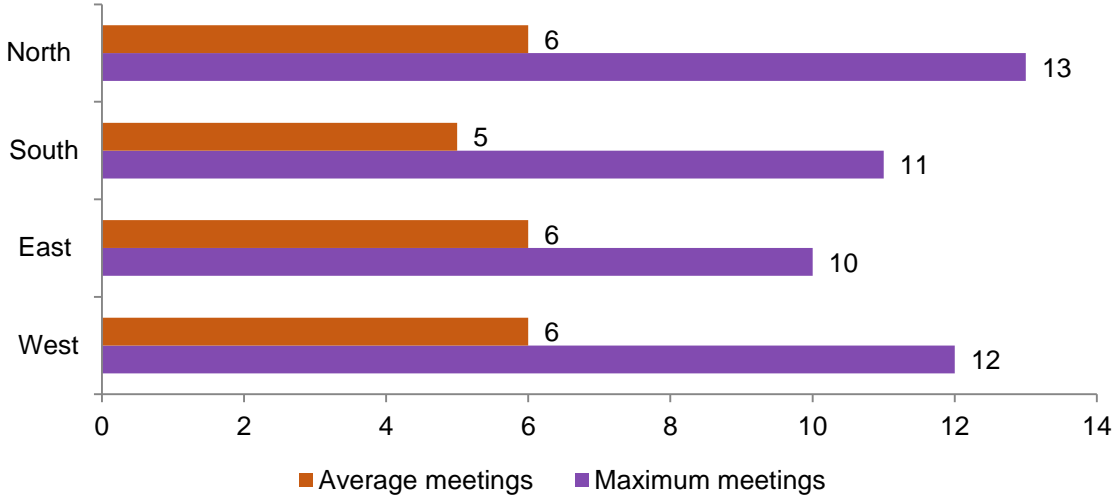


Meetings and attendance

Audit Committee meetings and attendance

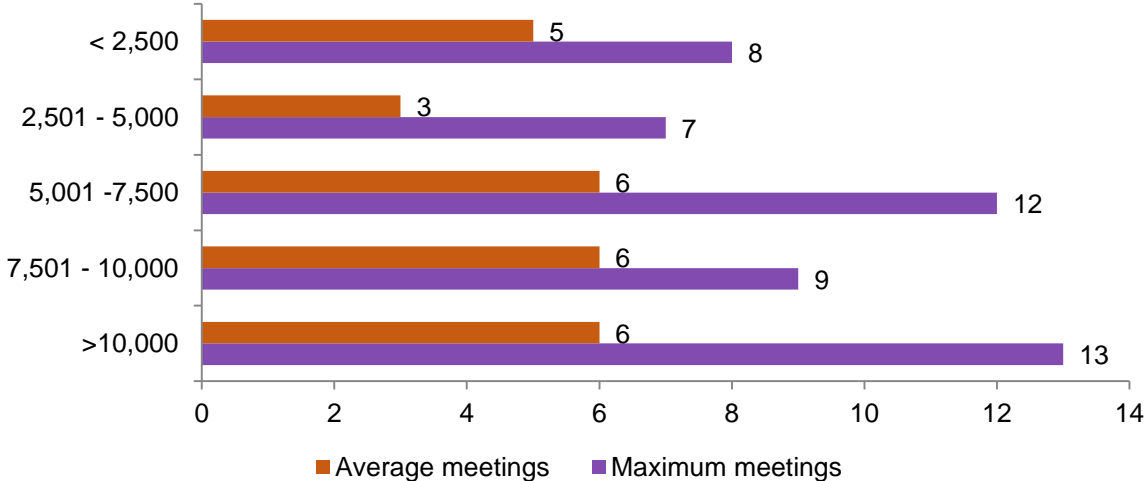
Maximum and average number of Audit Committee meetings

B. Region-wise analysis



Maximum and average number of Audit Committee meetings

C. Company turnover-wise analysis (INR crores)

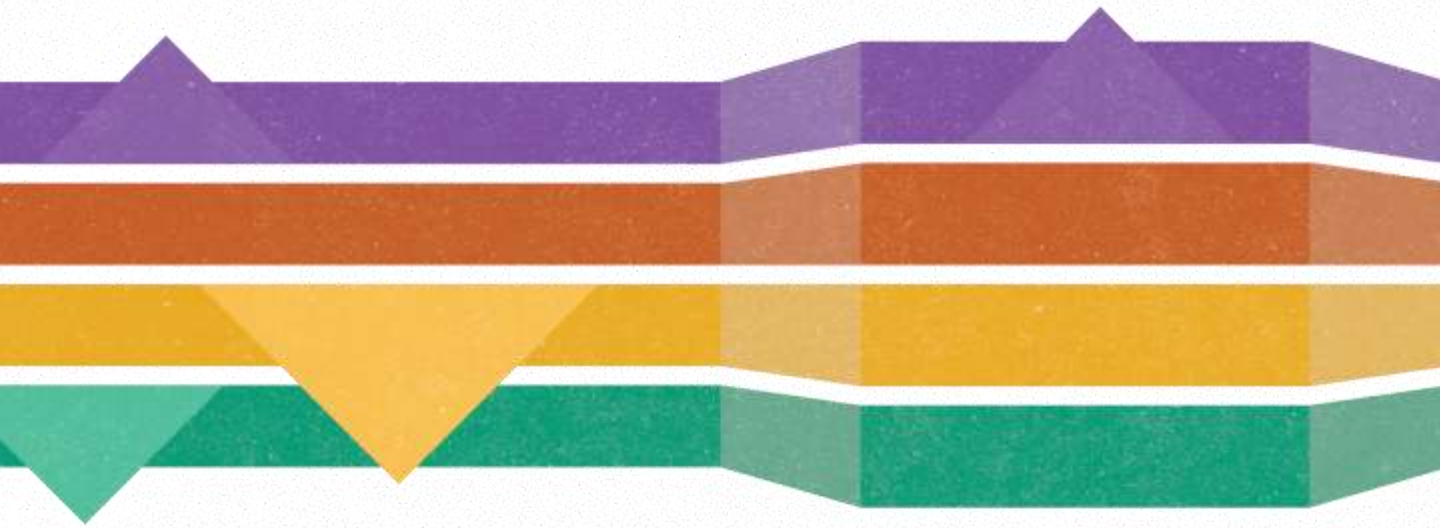


Average attendance of directors at Audit Committee meetings was 83% [85%].

Average attendance of independent directors at Audit Committee meetings was 72% [83%].

5

Independent and Nominee directors



5.1 Independent directors



Independent directors

To protect the interest of minority shareholders, the roles and responsibilities of independent directors have been significantly enhanced under RC 49 and the 2013 Act. Many provisions are also aimed at mitigating actual or perceived threats to independence and objectivity of directors.

The 2013 Act defines who is an ‘independent director’ and provides tenure of five years to them in office, with a reappointment option for an additional five years by passing a special resolution.

A cooling period of three years has also been mandated before the next appointment. Tenure under the 2013 Act and RC 49 are applicable with prospective effect.

As per RC 49, an individual can be an independent director in maximum of seven listed companies. Further, if he/ she is also serving as a whole-time director in any listed company, then he/ she can be an independent director in a maximum of three listed companies.

To enhance transparency and to provide relevant information to shareholders, companies may consider publishing the above mentioned aspects about independent directors in their annual reports.

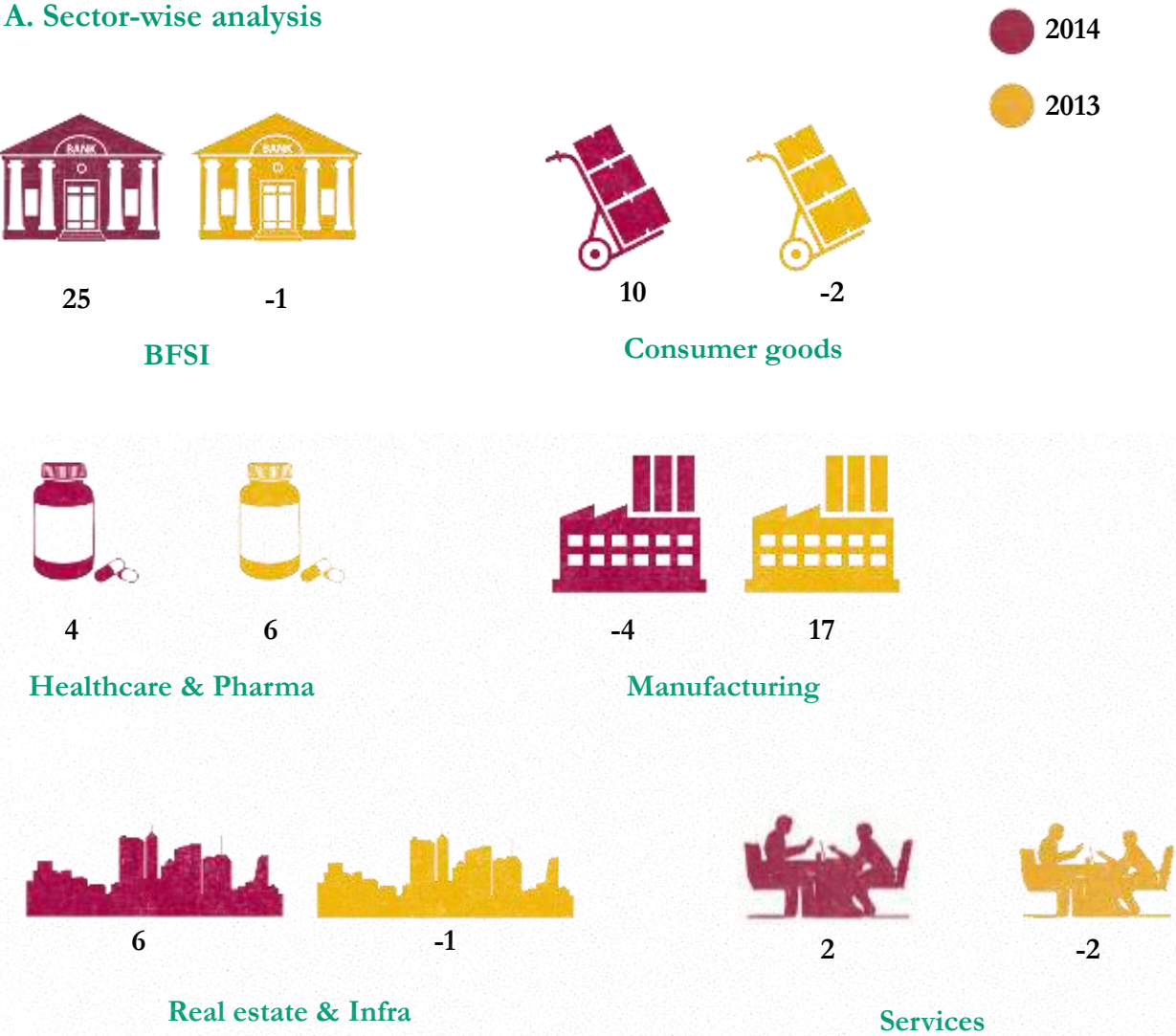
144 [134] independent directors were inducted and 101 [117] resigned from the Board during the previous financial year. Net increase of independent directors from 17 to 43 indicates a positive move towards an independent Board.



Independent directors

Net appointment of independent directors

A. Sector-wise analysis



BFSI is leading the way in terms of the appointment of independent directors, with 25 net appointments

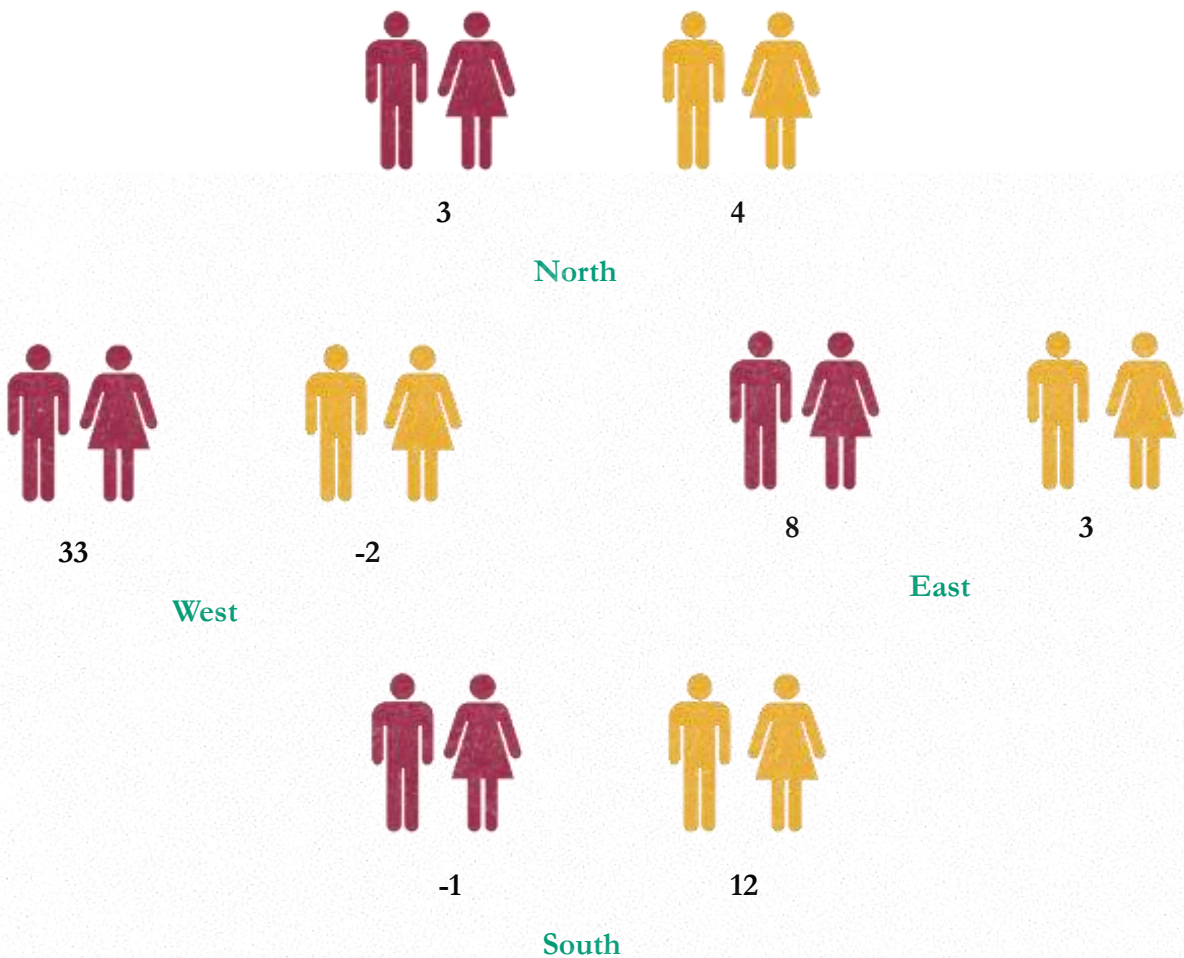
Independent directors

Net appointment of independent directors

B. Region-wise analysis

● 2014

● 2013



Significant appointments were noted in the West, with 33 net appointments

Independent directors

Net appointment of independent directors

C. Company turnover-wise analysis (INR crores)



-1



2

< 2,500



6



-6

2,501 - 5,000



10



-2

5,001 - 7,500



-3



0

7,501 - 10,000



31



23

>10,000



Companies that have turnover exceeding INR 10,000 crores witnessed the maximum appointment of independent directors

Independent directors

RC 49 of the Listing Agreement has mandated new requirements such as issue of appointment letter, publication of terms and conditions of appointment on company website, performance evaluation, conducting exclusive meetings for independent directors, publication of familiarisation programs on company website and link in the annual report, and restriction of stock option for independent directors.

Just 21 companies reported of having held "independent directors' only" meetings in their annual report.

Of the above, 14 companies have a turnover of over INR 10,000 crores and 11 of these companies are from the western region.

As per the 2013 Act, declaration of independence has to be obtained from independent directors during the first Board meeting after appointment and in the first Board meeting of every financial year.



5.2 Nominee directors



Nominee directors

Nominee directors are those directors that are nominated by any financial institution or by any agreement. Besides, they can be appointed by any government or by any other person to represent their interest.

The 2013 Act and RC 49 exclude nominee directors from being considered as independent directors.

46

out of the 150 companies have considered 107 nominee directors as independent directors.

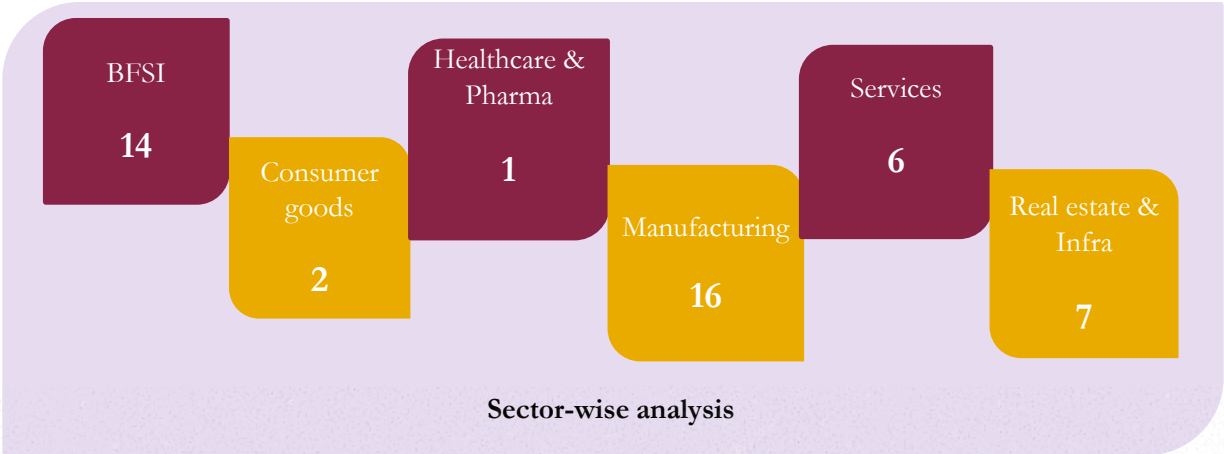
15

(83%) out of the 18 public sector companies have considered 25 nominee directors as independent directors.

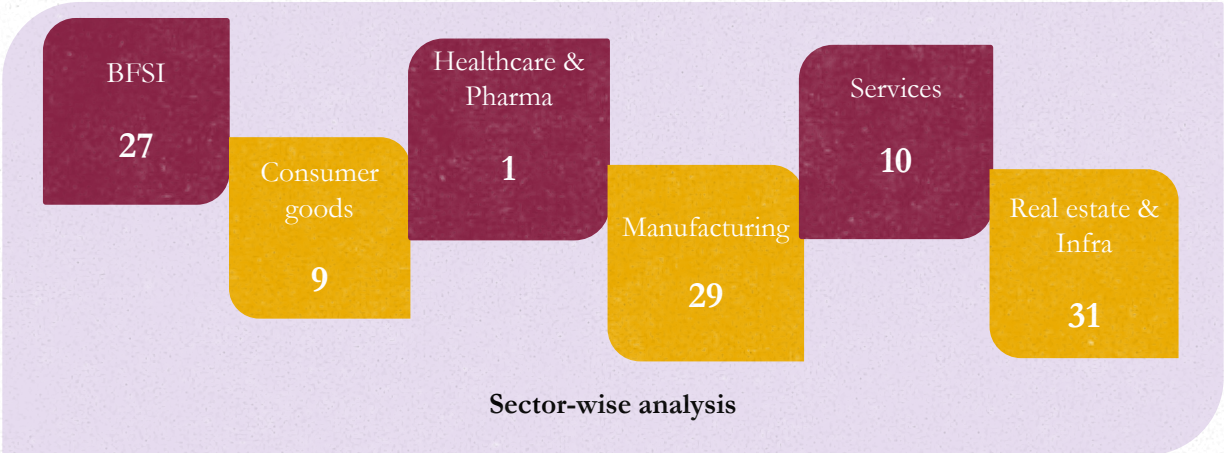


Nominee directors

Number of companies that have considered nominee directors as independent directors



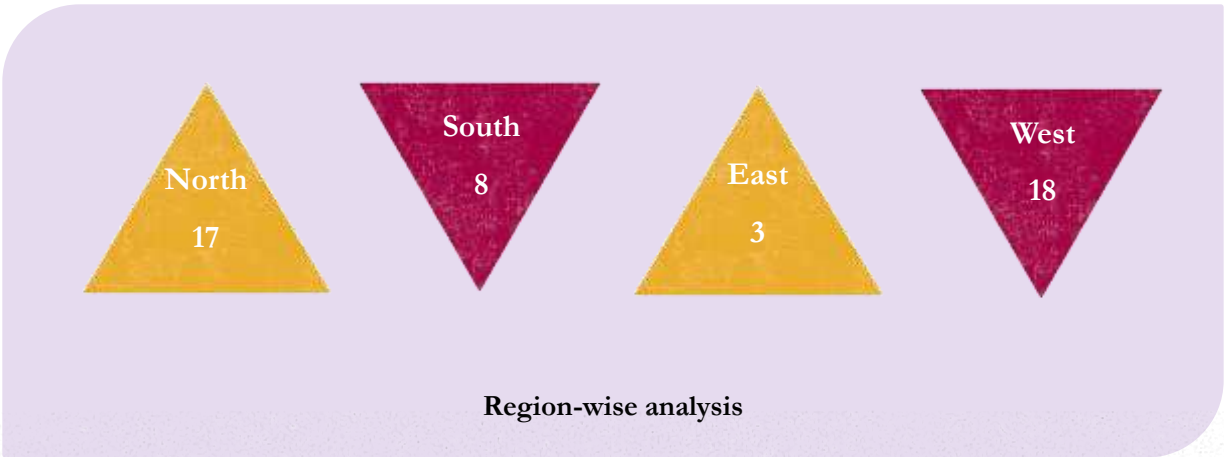
Number of nominee directors considered as independent directors



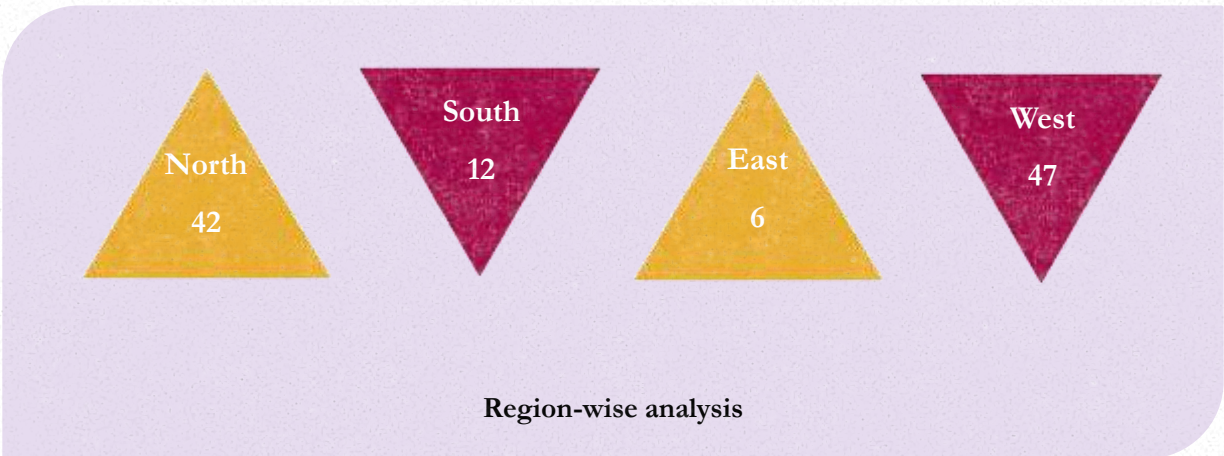
Companies in the BFSI sector (14 companies, 47%) lead the way, followed by companies in the manufacturing sector (16 companies, 33%), in terms of considering nominee directors as independent directors

Nominee directors

Number of companies that have considered nominee directors as independent directors



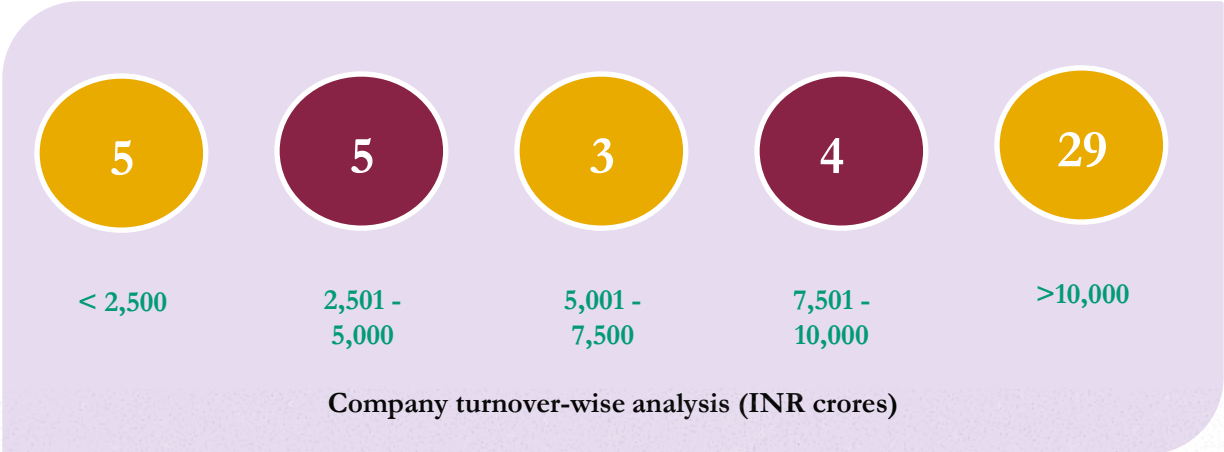
Number of nominee directors considered as independent directors



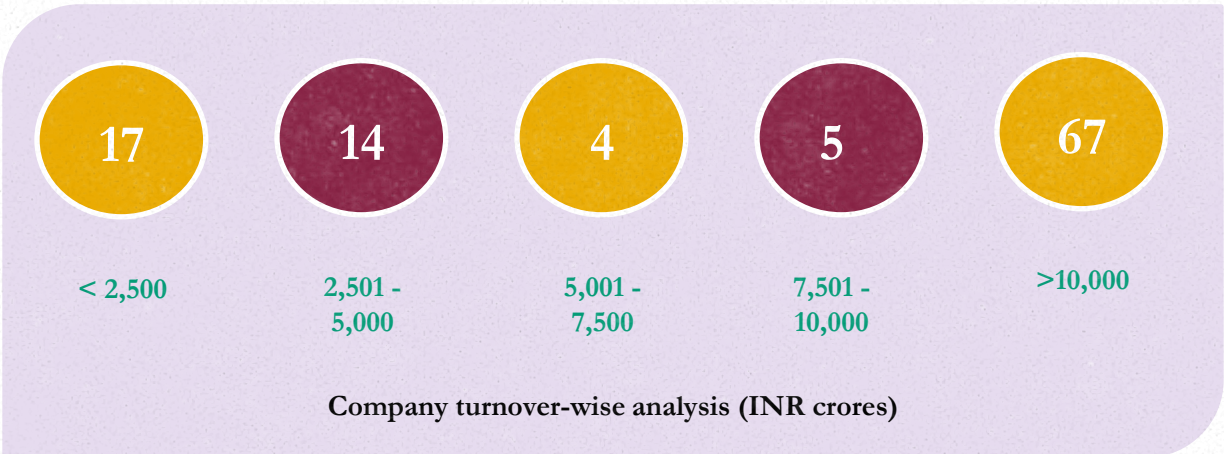
17 companies (49%) in the northern region have considered nominee directors as independent directors

Nominee directors

Number of companies that have considered nominee directors as independent directors



Number of nominee directors considered as independent directors



29 companies (45%) that have turnover exceeding INR 10,000 crores have considered nominee directors as independent directors

Expert view



Statutory independent regulators like Telecom Regulatory Authority of India (TRAI) and Tariff Authority for Major Ports (TAMP) were expected to bring decisions taken in private by government officials, into the open such that these are then taken in a transparent and consultative manner. However, each Ministry set up its own regulatory body. There are gaps between the different regulatory commissions on each of the major issues: independence and autonomy, their empowerment, accountability, transparency and public participation and enhancement of the quality of professional inputs for the regulatory bodies, functions and relationships with the concerned ministries.

True independence demands that selections for regulatory bodies must not be ad-hoc standing committees. There should be no delays in constituting them, which would postpone (as they have repeatedly done) the selection process. Statutory selection committees must not be composed primarily of current or ex-bureaucrats but of others such as sitting or retired superior court judges nominated by a Chief Justice, directors of reputed institutions like the Indian institutes of technology (IITs), lok ayuktas, etc. Not more than one current or retired government official, if at all, must be selected.

The government's directives to the regulatory bodies must be transparent and restricted to ensure minimal interference in the work of the bodies. The primary accountability of the regulatory body should be to the concerned legislatures. Government audits of regulatory bodies must be only of the expenditures, not of their decisions or their financial effects on the government. All proceedings of the regulator should be translated into local languages and made available to the public, if necessary, by suitably pricing them, and by publishing them on the website. Objectives of regulatory bodies must have common features, encourage, even stimulate, competition; simulate competition in natural monopolies, examine efficiency of operations and capital employed, etc.

The present structure of independent regulatory bodies has developed in a haphazard manner. This new institution of governance enables public involvement through transparent functioning, involves all stakeholders in decisions that affect them and ensures accountability by justifying all decisions.

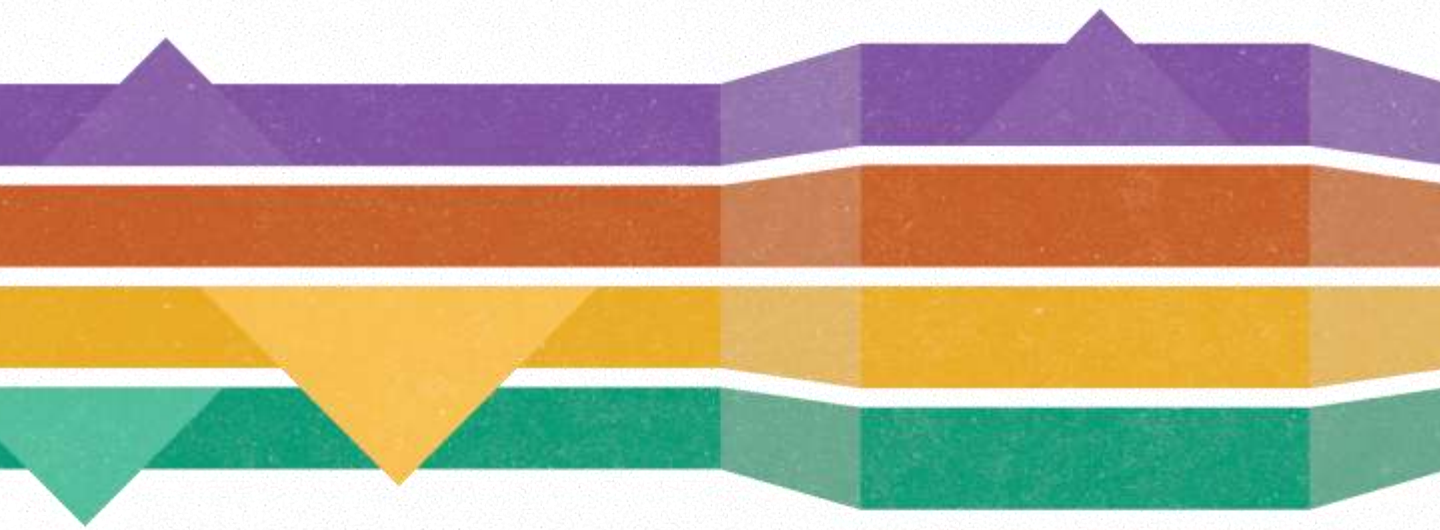


S L Rao
Former director-general,
NCAER and First Chairman,
CERC



6

Risk management



Risk management

Board of directors' report must include a statement indicating development and implementation of a risk management policy for the company. The statement must include identification of the elements of risk, if any, which, in the opinion of the Board, may threaten the existence of the company.

RC 49 makes the Board responsible for framing, implementing and monitoring the risk management framework, which is a significant change from C 49 where the primary responsibility was on the company and the Board was required to just be aware of the risks.

Audit Committee is also responsible for evaluation of the risk management mechanism.

Independent directors should ensure that risk management mechanism is robust and operational.

- All companies reported that they have complied with C 49 requirements, which indicates that their Audit Committees' review the risk management process
- 69 companies have specifically mentioned that their Audit Committees review the risk management framework

A. Sector-wise analysis

Number of companies: 69

% indicates percentage of companies within the sector
 Figures in brackets () indicate number of companies



40%
(12)

BFSI



59%
(10)

Consumer goods



24%
(4)

Healthcare & Pharma



46%
(24)

Manufacturing



41%
(7)

Real estate & Infra



71%
(12)

Services

Risk management

B. Region-wise analysis

Number of companies: 69

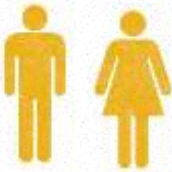
% indicates percentage of companies within the region

Figures in brackets () indicate number of companies



51%
(18)

North



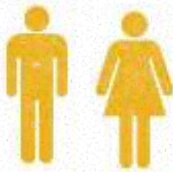
47%
(37)

West



33%
(3)

East



41%
(11)

South

Risk management

C. Company turnover-wise analysis (INR crores)

Number of companies: 69

% indicates percentage of companies within the turnover range

Figures in brackets () indicate number of companies



45%
(10)

< 2,500



40%
(14)

2,501 - 5,000



45%
(5)

5,001 -7,500



44%
(7)

7,501 - 10,000



50%
(33)

>10,000

Risk management

Risk management committee

RC 49 requires top 100 listed companies by market capitalisation, as at the end of the immediate previous financial year, to constitute a Risk Management Committee ('RMC').

Further, majority of the Committee shall consist of members of the Board of Directors. The Chairperson shall also be a member of the Board of Directors.

34

companies out of 150 companies (24 companies out of top 100 listed companies by market capitalisation) have reported of constituting a RMC.

In all 34 companies, majority of Risk Committee members are Board of Directors. Further, in all 34 companies, Chairperson of the Committee is also a Board member.

Only four companies in the public sector have reported of constituting a RMC. Three out of the four companies are top 100 listed companies by market capitalisation.



Risk management

Companies constituting a RMC

A. Sector-wise analysis

Number of companies: 34

% indicates percentage of companies within the sector

Figures in brackets () indicate number of companies



77%
(23)

BFSI



0%
(0)

Consumer goods



12%
(2)

Healthcare & Pharma



10%
(5)

Manufacturing



6%
(1)

Real estate & Infra



18%
(3)

Services



BSFI is leading the way in terms of having a risk management mechanism, as 23 companies (77%) have reported of constituting a RMC

Risk management

Companies constituting a RMC

B. Region-wise analysis

Number of companies: 34

% indicates percentage of companies within the region

Figures in brackets () indicate number of companies



17%
(6)

North



20%
(16)

West



22%
(2)

East



37%
(10)

South

Risk management

Companies constituting a RMC

C. Company turnover-wise analysis (INR crores)

Number of companies: 34

% indicates percentage of companies within the turnover range

Figures in brackets () indicate number of companies



5%
(1)

< 2,500



6%
(2)

2,501 - 5,000



18%
(2)

5,001 - 7,500



31%
(5)

7,501 - 10,000



36%
(24)

>10,000



36% of companies that have turnover more than INR 10,000 crores have reported of constituting a RMC

Risk management

- RMC met at least four times during the financial year
- Average attendance of directors at a RMC meeting stood at 73%
- The range of meetings was 1 to 7

Average number of risk committee meetings

A. Sector-wise analysis



4

BFSI



0

Consumer goods



4

Healthcare & Pharma



3

Manufacturing



1

Real estate & Infra



4

Services

With enhanced requirements of risk management process, we expect that companies will implement a robust risk management framework in the coming years and report more details on how they have institutionalised Enterprise Risk Management ('ERM') framework in their companies.

The Board's role is to provide entrepreneurial leadership to the company with a framework of prudent and effective controls which enables risk to be assessed and managed.

- UK Corporate Governance Code



Institutionalising Enterprise Risk Management: Key success factors and common mistakes

Unlocking the potential of an opportunity by taking calculated risks plays a significant role in the success of a business. At the same time, top of the mind question in the wake of recent corporate scandals and decline of large conglomerates is 'did the company have an adequate risk management mechanism?'

In this highly connected and dynamic world, several factors such as regulatory environment, macroeconomic business environment, competition, demography, culture, customer preferences, supply chain, etc., impact the success of the business. Rapid changes in these factors are only adding to these challenges and pose risks to the success of any business.

Companies do identify risks and define mitigation measures to bring them to an acceptable level but key question to be asked is "is it a structured, continuous and consistent approach at an enterprise level, involving all key stakeholders of the organisation?"

The answer to this question lies in 'Institutionalising' an ERM framework in the company.

ERM is a major line of defence as well as a key governance measure. A well implemented ERM framework will guide an organisation in mitigating and managing risks, which otherwise can materially affect the organisation's ability to achieve its stated objectives.

Key success factors to institutionalise an ERM framework are:

- The Board sponsorship of ERM is critical to give the desired importance
- Involve all key stakeholders - Business heads, Operations, Support functions, etc.
- Embed identification and evaluation of risk in culture of the organisation
- Establish a transparent culture which encourages identification and deliberation on risks
- Periodically review risk profile for timely course correction
- Focus and prioritise key risks. Avoid developing laundry list of risks
- Focus on both external and internal risks
- Identify focus group to drive the framework rather than to identify risks

Finally 'Keep it simple!'

Common mistakes:

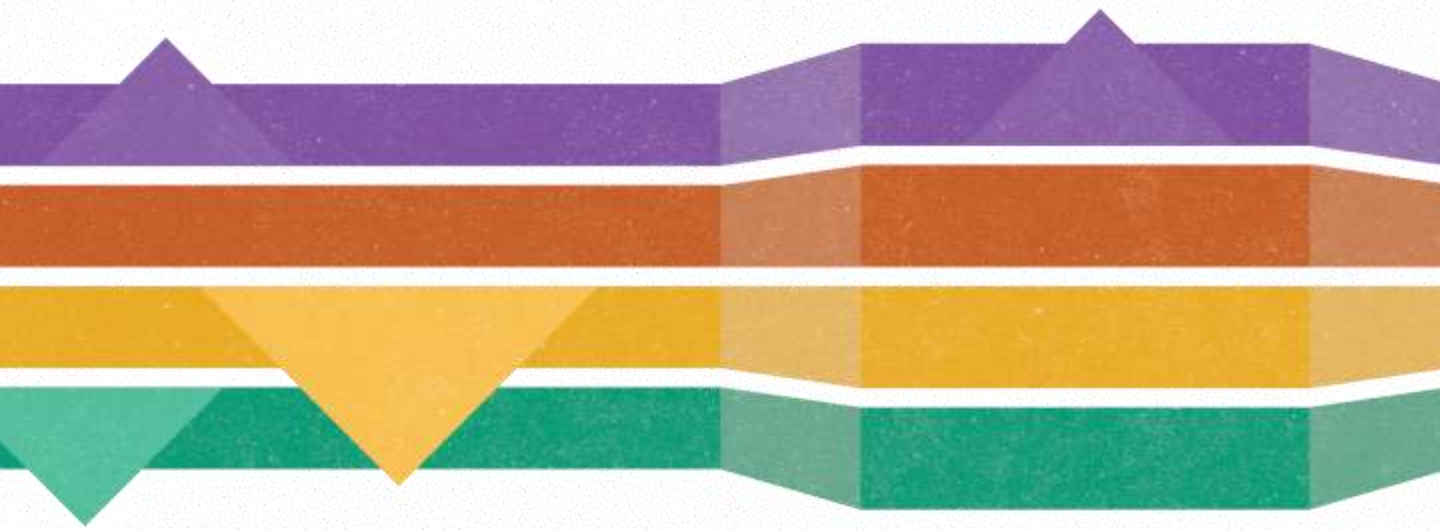
- Compliance focus
- Being seen as a finance function job/ part-time job/ one-time activity
- Giving undue importance to rating of risk than to the risk itself
- Assessing criticality of risk using only past data
- Giving undue importance to the probability of occurrence of risk rather than to evaluating the impact of risk, even if there is a remote chance of it occurring once
- Being considered as a hindrance to take risk

Bhanu Prakash Kalmath S J
Executive Director
Grant Thornton India LLP



7

Vigil/ Whistle blower mechanism



Vigil/ Whistle blower mechanism

RC 49 and the 2013 Act enable and encourage stakeholders to report any unethical practice to the Board which is a great step towards better corporate governance.

The 2013 Act mandates establishment of a vigil mechanism to safeguard against victimisation of employees and directors.

RC 49 has made whistle blower mechanism a mandatory requirement. As per the new law, companies shall establish a vigil mechanism for directors and employees to report concerns about unethical behaviour, actual or suspected fraud and violation of the company's code of conduct or ethics policy.



As a good practice, whistle blower mechanism should also cover external stakeholders like customers, vendors, contractors, etc.

85%

of 150 companies, i.e. **122 companies** have reported the existence of a vigil/ whistle blower mechanism in their annual report or on the company website.



Vigil/ Whistle blower mechanism

Companies that have a vigil mechanism

A. Sector-wise analysis

Number of companies: 122

% indicates percentage of companies within the sector

Figures in brackets () indicate number of companies



90%
(27)

BFSI



76%
(13)

Consumer goods



76%
(13)

Healthcare & Pharma



71%
(37)

Manufacturing



88%
(15)

Real estate & Infra



100%
(17)

Services

100%

of the companies in the service sector have published vigil mechanism in their annual reports or on the company websites.

Vigil/ Whistle blower mechanism

Companies that have a vigil mechanism

B. Region-wise analysis

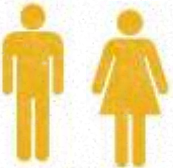
Number of companies: 122

% indicates percentage of companies within the region
Figures in brackets () indicate number of companies



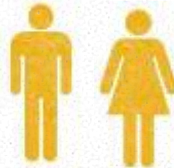
69%
(26)

North



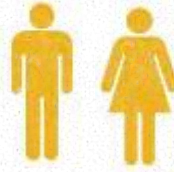
55%
(67)

West



50%
(6)

East



48%
(23)

South

Vigil/ Whistle blower mechanism

Companies that have a vigil mechanism

C. Company turnover-wise analysis (INR crores)

Number of companies: 122

% indicates percentage of companies within the turnover range

Figures in brackets () indicate number of companies



82%
(18)

< 2,500



69%
(24)

2,501 - 5,000



64%
(7)

5,001 -7,500



88%
(14)

7,501 - 10,000



89%
(59)

>10,000

Additional measures mandated by the 2013 Act are:

- Stakeholders should be given access to the Chairperson of the Audit Committee
- Vigil mechanism policy should be published on the company website
- Vigil mechanism should be described in the Board's report

- Code for independent director states that the independent director has to ascertain and ensure that the company has an adequate and functional mechanism. Further, the independent director has to ensure that interests of a person who uses the mechanism is not prejudicially affected (Schedule IV of the 2013 Act)

Vigil/ Whistle blower mechanism

58

out of the 122 companies have described vigil mechanism in their annual reports or on the company websites.

Analysis of key aspects covered by these 58 companies in their whistle blower mechanism

1

Number of companies that have women representation on the whistle blower committee



34

Number of companies that have extended this facility to people beyond employees and directors



30

Number of companies that allow anonymous reporting



33

Number of companies that have E-mail and/ or Hotline facility to report complaints



Vigil/ Whistle blower mechanism

Analysis of key aspects covered by these 58 companies in their whistle blower mechanism

24

Number of companies that have appointed an Ombudsman



49

Number of companies that provide whistle blowers an access to the Audit Committee



34

Number of companies that have constituted a whistle blower committee



30

Number of companies that cover acts of bribery or corruption in their whistle blower mechanisms



10

Number of companies that cover aspects of gifts and hospitality expenditure



Vigil/ Whistle blower mechanism

Analysis of vigil mechanism in the 58 companies

A. Sector-wise analysis

% indicates percentage of companies within the sector
Figures in brackets () indicate number of companies



43%
(13)

BFSI



53%
(9)

Consumer goods



47%
(8)

Healthcare & Pharma



35%
(18)

Manufacturing



18%
(3)

Real estate & Infra



41%
(7)

Services

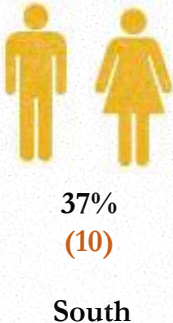
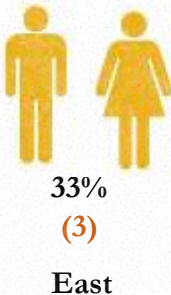
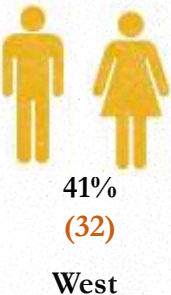
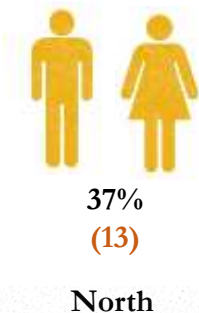


Vigil/ Whistle blower mechanism

Analysis of vigil mechanism in the 58 companies

B. Region-wise analysis

% indicates percentage of companies within the region
Figures in brackets () indicate number of companies



Vigil/ Whistle blower mechanism

Analysis of vigil mechanism in the 58 companies

C. Company turnover-wise analysis (INR crores)

% indicates percentage of companies within the turnover range
Figures in brackets () indicate number of companies



32%
(7)
< 2,500



49%
(17)
2,501 - 5,000



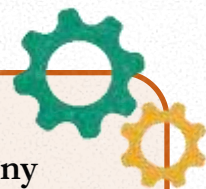
45%
(5)
5,001 - 7,500



56%
(9)
7,501 - 10,000



30%
(20)
>10,000



With vigil mechanism becoming mandatory, we expect that many companies will shortly strengthen and operationalise their whistle blower mechanism.

A practical approach to whistle blower mechanism

Companies can follow some simple procedures to ensure that whistle blowing policies are embedded within the overall risk and ethics framework and culture of an organisation. Some of the steps that companies can consider are as follows:

Top-level commitment

The CEO and the Board should clearly support and sponsor any whistle blowing regime. It should be ensured that the Board members or other senior managers respect the policy.

Senior accountability

A senior member of the management must be responsible for embedding the culture of internal disclosure throughout the company - particularly within the management. It should be the responsibility of this person to announce the policy to all employees, manage and review it, and provide feedback to the Board.

Communication and training

Employees must know that the company has a whistle blowing policy and understand when and how to use it. This can be ensured through regular E-mails, videos and presentations from the CEO or the legal counsel.

Regular review and audit

Regularly review any whistle blowing policies and prepare reports on the number and types of disclosures received in any given year.

Asking some of the questions, as below, will help your Board consider applying the policy more effectively.

- Are the disclosures widespread across the company or limited?
- Are the disclosures concentrated in a particular business area or scattered?
- Is the number of disclosures going up or down?
- Do employees feel capable and safe in making disclosures?
- Are the types of issues being disclosed appropriate and sensible?
- How have disclosures been investigated and followed up?

It is useful to give employees updates on a more general level. This enables them to see that people are making disclosures and that those disclosures are being dealt with appropriately. Details can be anonymised and used as examples of how to manage disclosures.



A practical approach to whistle blower mechanism

Proper investigation and action

It is essential that the whistle blowing policy is enforced. To ensure that the efficacy of the policy remains intact, it is essential that all disclosures are investigated promptly and properly. Keep the whistle blower informed at all times and as much as possible. You could use this opportunity to reassure the whistle blower and explain that the investigation is progressing but, due to confidentiality, no further information can be given.

This would serve as an encouragement to the whistle blower that the disclosure is being taken seriously and there is no need to disclose the matter elsewhere – to the media or the regulators, for example.

Feedback

Ask employees about their views on the whistle blowing policy and its effectiveness. You could include questions, such as the ones below, in an employee satisfaction or feedback survey.

- Have you read the whistle blowing policy?
- Do you know who to contact if you want to make a disclosure?
- Do you feel you work in an open environment wherein you are encouraged to safely voice any concerns?
- What would you like to change about the policy?



Vidya Rajarao

Partner

Grant Thornton India LLP

8

Auditors



Auditors

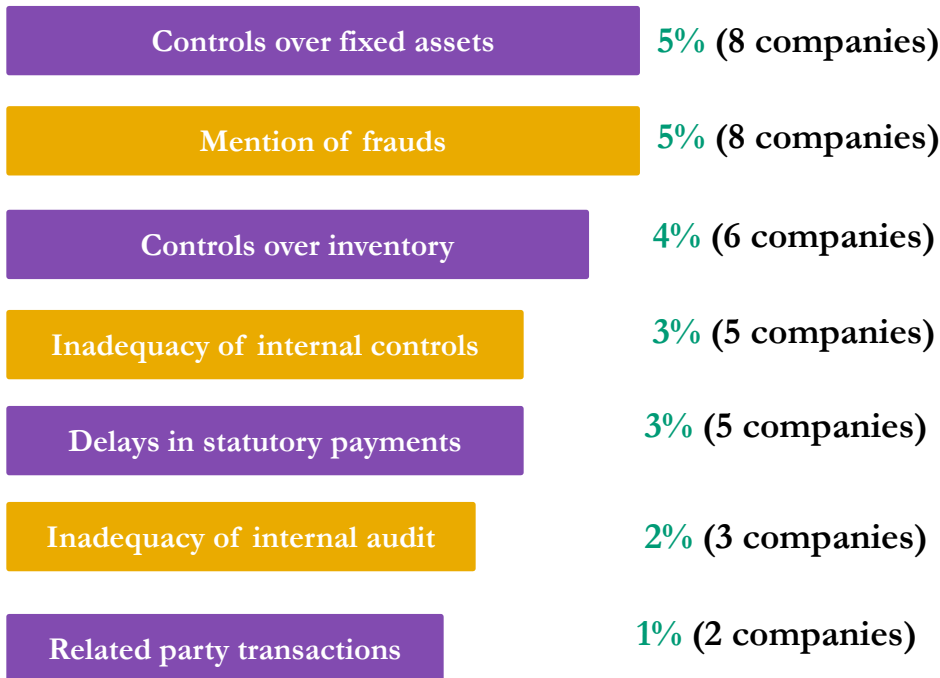
Auditors' report

- Auditors have qualified audit opinion of six out of 150 companies
- Auditors of 50 companies have drawn attention of stakeholders to specific matters in the audit reports

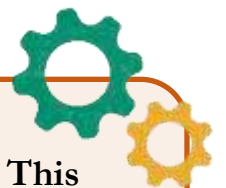
CARO mandates auditors to comment on aspects of bookkeeping, managing fixed assets, inventory, internal controls, statutory payments and fraud.

Analysis of the Annexure to CARO requirement indicated that auditors have commented on controls over fixed assets, inventory, inadequacy of internal audit and controls, etc.

Summary of auditors' comments by area



The 2013 Act has given statutory recognition to internal audit. This statutory recognition will strengthen powers and also increase responsibilities of this key pillar of corporate governance.



Emerging trends in Internal Audit

In this ever dynamic economic environment, businesses are continuously evolving and very rapidly at that. Much like other functions, the internal audit function too needs to continuously evolve and be nimble to adapt to the changing scenario. To achieve this, it is imperative for the internal audit function to align itself to the businesses strategy and transform itself rapidly.

A key emerging trend in the C-suites and boardrooms is to perceive internal audit as a trusted and strategic advisor. To remain in this sphere, the internal audit function should move away from traditional audit areas and focus on a plan that provides the right mix of assurance, compliance and consulting engagements.

Although the function does not get involved in setting strategies, it can contribute to the cause by reviewing the effectiveness of implementation of strategies. The caution, however, is that in playing an advisory role, internal auditors have to ensure that they are not involved in the decision-making on design of processes or in any other way that may be a conflict later while they review the business.

With the rapidly changing technological environment and copious amounts of data being captured, it has become increasingly important for internal auditors to embrace the use of data analytics. Usage of data analytics to provide the management and the Boards a real-time view of risks would prove to be huge differentiator. On the softer side, it is imperative to embed analytics as a part of the function's methodology and DNA.

Collective skills and competencies have always been core attributes for defining an effective internal audit function. In recent times another attribute that is emerging as key is to be innovative and creative. Business models are getting creative so internal auditors need to be too. It has become imperative for hiring managers to not create clones in the department but rather to have on-board auditors with attributes different from those that already exist. Seeking out variety in the staffs' attributes and abilities will help the function become creative and avoid being typecast in their approach and thinking. It can be, at times, very useful to induct auditors who have prior experience of business operations.

The emerging trends, needless to say, pose several challenges for Chief Audit Executives ('CAEs') to wade through such as budget constraints, getting a seat at all relevant tables, shortage of resources, etc. That said, with continuous engagement and by showcasing the value proposition of the function, CAEs can remain relevant in the grand schemes of an organisation effectively.

Lav Goyal
Partner
Grant Thornton India LLP



Auditors

The 2013 Act has mandated the establishment of Internal Financial Controls (IFCs) framework in the company to ensure orderly and efficient conduct of its business, including adherence to the company's policies, safeguarding its assets, prevention and detection of frauds and errors, accuracy and completeness of accounting records, and the timely preparation of reliable financial information. Key provisions are:

- Directors have to confirm, in the responsibility statement, that there are internal controls over financial reporting and that such controls are working effectively

- The Statutory Auditor should state whether the company has an adequate internal control system in place
- Audit Committee may call for comments from the Statutory and Internal Auditors of the company about the efficacy of the internal control system

Consolidated financial statements

The 2013 Act mandates all companies, which have one or more subsidiaries, to prepare consolidated financial statements.

139

out of 150 companies have published consolidated financial statements as a part of their annual report.



Auditors

Fraud reporting

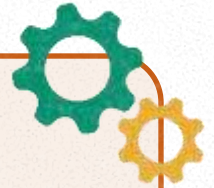
The 2013 Act mandates the auditor to inform the Central Government, within 60 days, if he/ she has reason to believe that a fraud is being committed or has been committed against the company by its employees or officers.

The 2013 Act and the Rules therein prescribe time limits for submitting the report to the Board/ Audit Committee, receiving responses and for sending the report to the Central Government.

8

companies' Auditors' Report have reference to the occurrence of fraud in the company.

We expect that companies will strengthen fraud prevention and identification measures in the short-term.



The Audit revolution: Mandatory firm rotation

As the management and corporate Boards consider changing their auditors, what should they look out for in their new auditor? Is it institutional acceptance, the size or the potential global reach, knowledge and skills or ability to understand the business?

Firstly, although technical competence of the auditor is important, in the current scenario, this criterion can be taken as table stakes. Every auditor must know the technicalities of his job, just as every CFO must know his. Same goes for institutional acceptance. Today, a large number of auditors and firms have gained acceptance by the Boards and institutional investors, and hence the name of the auditor and/ or the firm cannot be considered as a differentiator while making decisions.

Secondly, the law has significantly expanded the restrictions on the non-audit services that auditors can provide. In addition, the law has defined the restrictions on audit firm partners or their relatives extensively from holding securities in their clients' businesses. Does the prospective auditor have a real time system to capture this information and ensure that independence breaches are identified/ cleared?

Thirdly, what is the prospective auditor's quality control system. In addition, how does the auditor ensure compliance with the stringent quality standards demanded by the regulators?

These are the minimum requisites with which every auditor must ensure adherence. Hence, what should be the differentiating factors in this selection? Corporates demand value for money and what could be that value?

To begin with, the auditor's understanding of the industry and how this can impact the audit process should be considered. Like businesses, accounting and financial reporting frameworks have also become extremely complex, global and innovative. An auditor who understands the business is more likely to perform a more focused audit and actually provide value to corporates by making the audit more efficient, while also highlighting areas of improvement in the process.



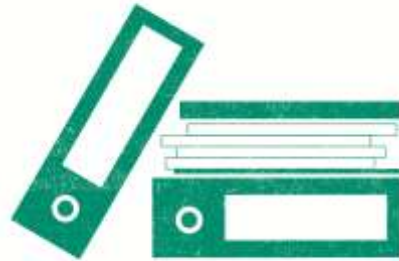
The Audit revolution: Mandatory firm rotation

The next crucial factor is the immediate team which will be constituted to service the company? While an audit firm may have hundreds of employees, it is the immediate service team with which the management will interact on a regular basis. Does that team have the understanding to manage a company and provide tailored services suited to match its size and unique nature of operations? Do they have prior experience to understand corporate expectations and can they deliver on their promise?

Thirdly, is the incoming auditor proactive or reactive? Does he work towards a solution or does he leave the company unguided to find its way through the maze? Independence is sacrosanct but auditors should be able to discuss a solution within the overall independence framework.

Lastly, is the auditor able to service the needs of a corporate? Are the auditors agile enough to give their views in a timely manner which may not necessarily be what the company would like to hear?

Companies and Audit Committees could do well by thinking of a potential shortlist and a robust process for selection. Further, if appropriate, they should consider a switch at some subsidiaries in order to work with multiple firms and assess which of these best meet their expectations, before making the change at the group level.



Aasheesh Arjun Singh
Partner
Walker Chandiook & Co LLP



Internal Financial Controls: Approach to compliance

The 2013 Act requires the director's responsibility statement to state that the directors, in the case of a listed company, had laid down IFCs to be followed by the company and that such IFCs are adequate and operating effectively. Further, the 2013 Act also requires the auditors' report to state whether the company has adequate IFC system in place and if these controls are operating effectively. Under management's responsibility, the 2013 Act has significantly expanded the scope of internal controls to be considered by the management of companies to cover all aspects of operations of the company. For auditors, whilst the scope for reporting the IFC is significantly larger and wider than the reporting under the CARO requirements, as clarified by the Institute of Chartered Accountants of India (ICAI) in its guidance note, it is implied that the auditor's assessment has to be limited to internal controls over financial reporting only.

Implementing the requirements will have its own sets of challenges related to people, processes, technology, and most importantly, to the cost. Though the costs are not easy to estimate, but we know that it is even tougher to quantify the benefits. However, given the massive financial scandals, decline in market capitalisation and resulting loss of investor confidence in our markets, it is believed that, of all of the recent reforms, the internal control requirements have the greatest potential to improve the reliability of financial reporting. This being said, companies should be encouraged to develop internal control roadmap to specifically address the needs of scale and complexity, and size of their businesses.

Also, after setting-up the initial framework, a lot can be achieved by re-organising the existing internal audit function in the organisations. This being an ongoing requirement, internal audit plan can be re-aligned to cover certain aspects, especially the operational areas, to provide support to the management in making their assessment.

It has been over a decade since the SOX requirements were laid down by the US Securities and Exchange Commission (SEC) and there is enough that could be learnt from the implementation experience of the US companies. Few such challenges for consideration are:

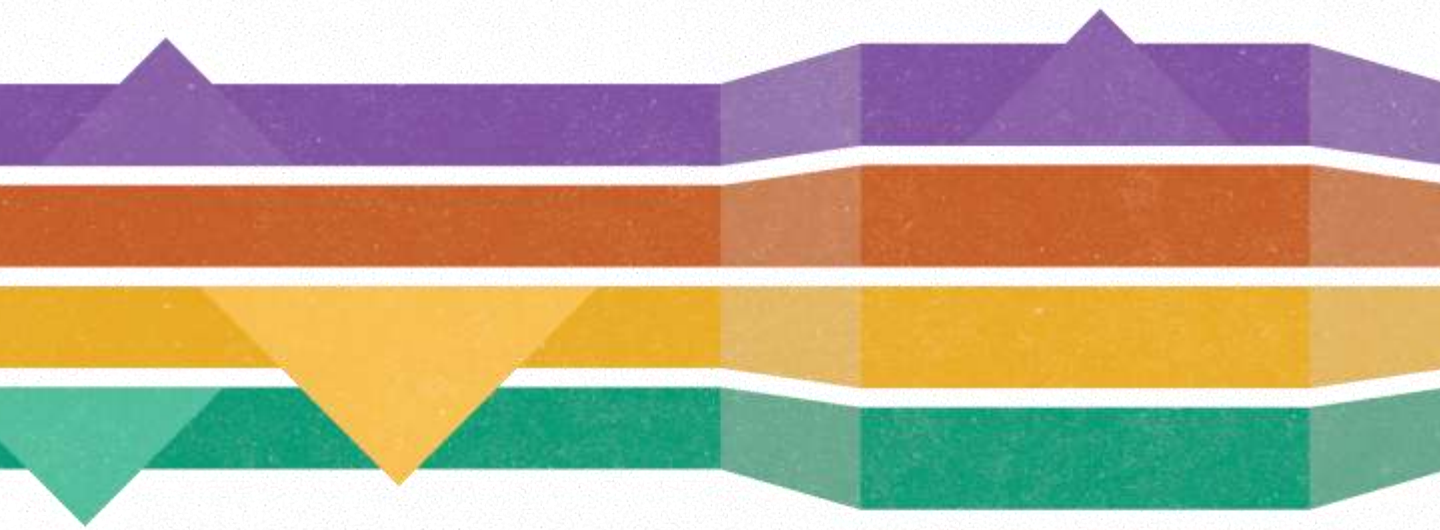
- Developing an effective strategy to test and evaluate entity-level controls
- Identifying all significant accounts and disclosures and significant processes
- Addressing multi-location issues
- Identifying IT processes that are integral to business processes
- Addressing issues associated with outsourced processes
- Consistency of documentation
- Lack of trained resources to perform review of documentation/ process flow
- Determining the appropriate level of documentation
- Determining an effective and efficient testing approach
- Determining an approach to appropriately identify and react to control exceptions
- Determining the process for identifying, documenting, communicating, and remediating control deficiencies

Shalabh Saxena
Partner
Grant Thornton India LLP



9

Related parties



Related parties

The 2013 Act mandates increased transparency in dealing with related parties. Audit Committee and the Board are responsible for ensuring that related party transactions are at arm's length.

Key provisions are:

- All related party transactions which are not in the ordinary course of business or not at arm's length basis should be approved by the Board
- Approval of shareholders can be sought by way of special resolution for contract, arrangement or transactions exceeding the prescribed amount or for companies with prescribed share capital. Related party shareholders are not permitted to exercise their voting rights, in such case of special resolution
- The company shall not make investments with more than two layers of investment companies, unless the investments are in an overseas company and the company has overseas subsidiaries, and such layers are permitted under the local law of the company being acquired or under the law of the acquiring company

RC 49 requires companies to define a policy for related party transactions. All related party transactions require prior approval of the Audit Committees. However, the Audit Committee can define a methodology and grant omnibus approval for related party transactions. Further, material related party transactions (if aggregate of all transactions, during a financial year, with the related party, exceeds 10% of annual consolidated turnover) require shareholders approval through a special resolution.

However, Audit Committee and prior shareholder approval through special approval is not needed for transactions between two government companies and between a holding and its wholly-owned subsidiary whose accounts are consolidated.

Companies have to publish policies relating to related party transactions on their website and the website link has to be given in the annual report for reference.

While all companies broadly reported that they have complied with C 49 requirements, 100 companies have specifically mentioned in their annual report that their Audit Committees review related party transactions.

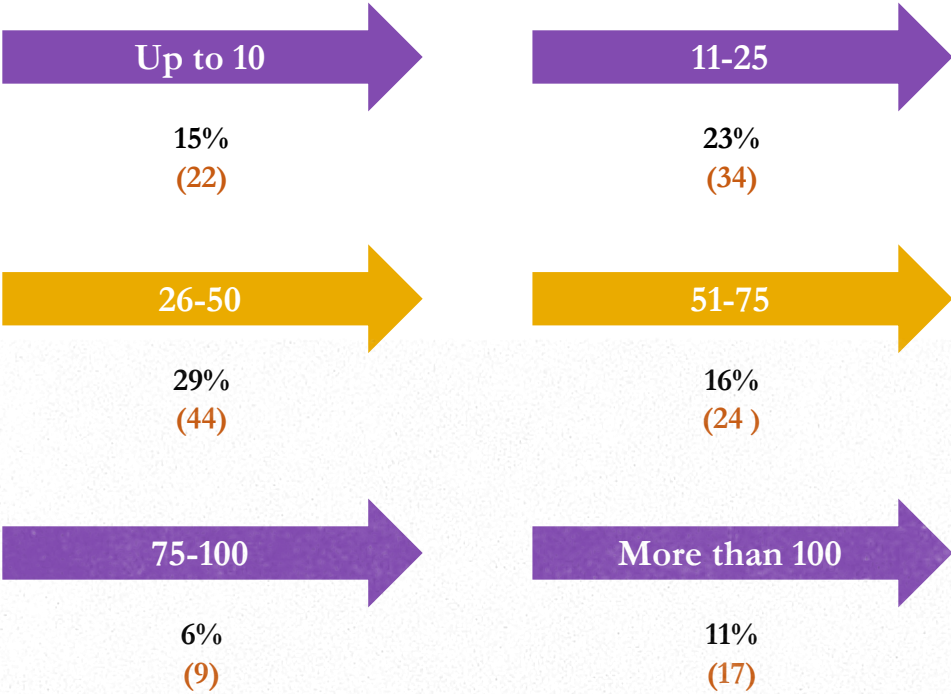
Annual report of one company mentioned that related party transactions are approved by the Audit Committee.

Average number of related parties reported by 150 companies was 52.

Related parties

Range of related parties reported by 150 companies (in percentage):

Figures in brackets () indicate number of companies



Related parties

Average number of related parties per company

A. Sector-wise analysis



21

BFSI



43

Consumer goods



50

Healthcare & Pharma



58

Manufacturing



106

Real estate & Infra



47

Services



Real estate & Infra sector had an average of 106 related parties per company, which is double the average of related parties of the 150 companies

Related parties

Average number of related parties per company

B. Region-wise analysis



59

North



30

East



44

South



55

West

Average number of related parties per company

C. Company turnover-wise analysis (INR crores)



40

< 2,500



66

2,501 - 5,000



26

5,001 - 7,500



45

7,501 - 10,000



56

> 10,000

10

Corporate Social
Responsibility



Corporate Social Responsibility

The 2013 Act mandates companies that meet certain criteria to contribute 2% of their net profit towards CSR activities, or provide reasons for non-compliance to the provisions of the 2013 Act. No penal provisions have been prescribed in case of non-compliance. However, the Board, in its report, needs to specify the reasons for not spending the specified amount.

The 2013 Act also mandates certain classes of companies to constitute a CSR Committee comprising three or more directors.

Detailed provisions on CSR and a prescribed format for sharing details of CSR initiatives in directors' report will encourage companies towards increased CSR disclosures in director's report.

148 companies have published information about their CSR activities in their annual reports or on their websites.

51 out of the above 148 companies have published information on constituting a CSR Committee.



Corporate Social Responsibility

Companies constituting CSR Committee

A. Sector-wise analysis

Number of companies: 51

% indicates percentage of companies within the sector

Figures in brackets () indicate number of companies



30%
(9)

BFSI



35%
(6)

Consumer goods



29%
(5)

Healthcare & Pharma



40%
(21)

Manufacturing



29%
(5)

Real estate & Infra



29%
(5)

Services

Corporate Social Responsibility

Companies constituting CSR Committee

B. Region-wise analysis

Number of companies: 51

% indicates percentage of companies within the region

Figures in brackets () indicate number of companies



46%
(16)

North



32%
(25)

West



22%
(2)

East



30%
(8)

South



Corporate Social Responsibility

Companies constituting CSR Committee

C. Company turnover-wise analysis (INR crores)

Number of companies: 51

% indicates percentage of companies within the turnover range

Figures in brackets () indicate number of companies



27%

(6)

< 2,500



26%

(9)

2,501 - 5,000



45%

(5)

5,001 - 7,500



25%

(4)

7,501 - 10,000



41%

(27)

>10,000



Of the above 51 companies, 9 companies (50%) are from the public sector and 21 companies (40%) are from the manufacturing sector

Paradigm shift from 'philanthropy' to 'impact per rupee spent' and compliance with the 2013 Act

A critical requirement for companies as per the CSR Rules, 2014 is reporting the evaluated and monitored performance of the CSR projects in implementation, as per the CSR policy defined by them. Considering an average economic growth rate of 6% to 7% in India over the next 5 years, at an estimated CSR baseline inflow of INR 18,000 to INR 20,000 crore in the first year, this sector is likely to be fuelled by approximately INR 1 lakh crore of funds in the next 5 years. The essence of CSR Rules is development for the amount spent.

This, therefore, triggers the debate on accountability of the money spent. With an aim to demonstrate transparency to their stakeholders, companies are now making a tectonic shift of switching over from the old concept of 'philanthropy' to 'sustainability of CSR programs'. This is compelling companies to measure the degree of improvement, thereby leading to revolutionary conversion of qualitative benefits into quantitative impacts, through the mechanism of 'Social Returns on Investment', to facilitate, in demonstration to their stakeholders, their accountability and thoughtful decisions taken for the money spent.

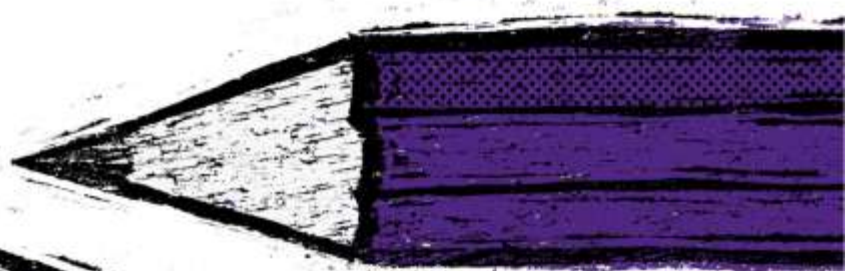
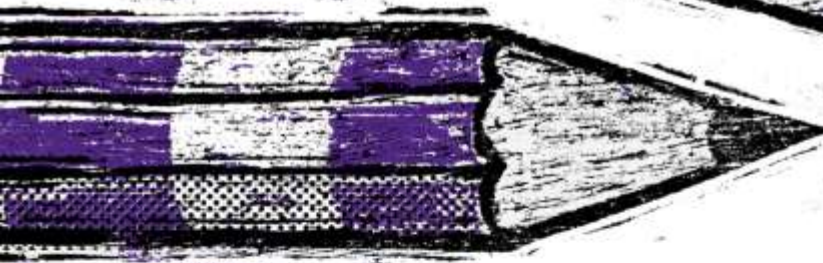
In this context, a lot of companies are welcoming the concept of audit of CSR projects. A special mention for such responsible and progressive companies which have anyways been practicing and encouraging an evaluation process through a third party for an audit of their CSR projects. Such companies have been evaluating and demonstrating the impact per rupee spent and challenging themselves to progress further, as per the widely accepted International Standard on Assurance Engagement (ISAE) 3000 released by the International Auditing and Assurance Standards Board.

Besides, obtaining an assurance from a competent third party facilitates in – (i) an affirmation of existence of an adequate and effective system and internal control for the CSR Rules, as against Section # 134 (5) (f) of the 2013 Act; and (ii) facilitates evaluation of the performance of the CSR Committee members, as per Section # 134 (3) (p) of the 2013 Act. This emerging need, combined with the requisite to demonstrate transparency on the impacts derived from the money spent, is also triggering the need of an audit guideline/ note from regulatory authorities, for facilitating companies to effectively monitor, evaluate and report their CSR performance and impacts. At the macro-economic level it makes a larger sense for the Government of India. Such third party endorsed reports will facilitate the capture and accounting of genuine information pertaining to various types of benefits incurred on account of large spends every year. And for the companies, apart from demonstrating their compliance, they get an access to genuine and endorsed good CSR projects, some of which may come at optimum cost, resulting in wider mileage. Overall, it's a win-win situation for every concerned stakeholder!

Rajib Kumar Debnath
Executive Director
Grant Thornton India LLP



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choose the
largest advisor.**



**Instinct says:
choose the
right advisor.**

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Our solutions

About Governance, Risk & Operations Advisory (GRO)

At Grant Thornton, we help businesses achieve the right balance between risk and reward by establishing an environment for timely and effective response to the ever changing business risks. We help our clients recognise and mitigate risks by setting up robust business processes, institutionalising the right internal controls, improving the use of information technology and achieving operational performance improvements. By proactively advising them to address and mitigate the unprecedented systemic risks affecting the control environment of their business, we create sustained value for our clients. Our range of services include:

- Internal audit
- Enterprise risk management
- Standard operating procedures
- Performance improvement
- Information technology
- SOC reporting
- Operational consulting
- Internal controls over financial reporting

About Governance Advisory Services

Companies need to understand the emerging governance regulatory environment and also to put the right corporate governance framework in place. As organisations seek to give stakeholders greater confidence, they face ever increasing pressure to demonstrate corporate governance good practices. We work with Audit Committee and Board of directors, as well as the management team, to develop bespoke solutions that strengthen governance structures which will underpin corporate performance as well as ensure regulatory compliance. Our suite of governance advisory services include:

- Clause 49 readiness
- CxO advisory
- Audit committee support
- Whistle blower mechanism
- Ethics review
- Forensic & investigation
- Compliance risk

About Board Advisory Services

Boards need specialist advice from time-to-time from experts and Grant Thornton is able to provide such advice. The areas in which we offer assistance to the Board include:

- Related party transactions
- Valuation
- Financial controls
- Vigil mechanisms
- Risk management
- Corporate Social Responsibility
- Compliance with accounting standards
- Forensic/ fraud investigations

For more information on our services, please visit us at: www.grantthornton.in/services

Should you have any queries or need our assistance in related matters, please write to us at

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