

# **Duties of Director - International comparision vis-a-viz India**

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### **Project Team Members**

## Chapter 1 : Duties of Board and Board Committees

*This chapter highlights duties of board and board committees. The chapter discusses the broad framework of the proposed research, methodology and research design.*

### Introduction

Corporate governance is the system by which companies are directed and controlled. **Corporate governance broadly refers to the mechanisms, processes and relations by which corporations are controlled and directed. These governance structures identify the distribution of rights and responsibilities among different participants in the corporation. Corporate governance includes the processes through which corporations' objectives are set and pursued in the context of the social, regulatory and market environment. Governance mechanisms include monitoring the actions, policies and decisions of corporations and their agents. Corporate governance practices are affected by attempts to align the interests of stakeholders.**

### Boards and Board Committees

Boards of directors are responsible for the governance of their respected companies. By appointing the directors and the auditors, boards always satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company's strategic objectives, providing the leadership, supervising the management, reporting mechanisms, managing shareholders rights, etc. The OECD has developed a Code

of Corporate Governance that would provide guidance to a number of key components of effective board practice. It is based on the underlying principles of all good governance: accountability, transparency, probity and focus on the sustainable success of an entity over the longer-term. High standards of transparency and accountability are needed to allow the public to assure itself that the state exercises its powers in accordance with the public's best interest. In OECD countries, the rationales for establishing or maintaining state enterprise ownership typically include one or more of the following: (1) the delivery of public goods or services where state ownership is deemed more efficient or reliable than contracting out to private operators; (2) the operation of natural monopolies where market regulation is deemed infeasible or inefficient; and (3) support for broader economic and strategic goals in the national interest, such as maintaining certain sectors under national ownership. According to OECD guidelines on Corporate Governance for the state owned enterprise (SOEs)<sup>1</sup>, the duties and responsibilities of Boards are detailed below:

- The boards of SOEs should be assigned a clear mandate and ultimate responsibility for the enterprise's performance. The role of SOE boards should be clearly defined in legislation, preferably according to company law. The board should be fully accountable to the owners, act in the best interest of the enterprise and treat all shareholders equitably.
- SOE boards should effectively carry out their functions of setting strategy and supervising management, based on broad mandates and objectives set by the government. They should have the power to appoint and remove the CEO. They

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<sup>1</sup> OECD Guidelines on Corporate Governance of State-Owned Enterprises, 2015, Edition

should set executive remuneration levels that are in the long term interest of the enterprise.

- SOE board composition should allow the exercise of objective and independent judgement. All board members, including any public officials, should be nominated based on qualifications and have equivalent legal responsibilities.
- Independent board members, where applicable, should be free of any material interests or relationships with the enterprise, its management, other major shareholders and the ownership entity that could jeopardise their exercise of objective judgement.
- Mechanisms should be implemented to avoid conflicts of interest preventing board members from objectively carrying out their board duties and to limit political interference in board processes.
- The Chair should assume responsibility for boardroom efficiency and, when necessary in co-ordination with other board members, act as the liaison for communications with the state ownership entity. Good practice calls for the Chair to be separate from the CEO.
- If employee representation on the board is mandated, mechanisms should be developed to guarantee that this representation is exercised effectively and contributes to the enhancement of the board skills, information and independence.
- SOE boards should consider setting up specialised committees, composed of independent and qualified members, to support the full board in performing its functions, particularly in respect to audit, risk management and remuneration. The



establishment of specialized committees should improve boardroom efficiency and should not detract from the responsibility of the full board.

- SOE boards should, under the Chair's oversight, carry out an annual, well structured evaluation to appraise their performance and efficiency.
- SOEs should develop efficient internal audit procedures and establish an internal audit function that is monitored by and reports directly to the board and to the audit committee or the equivalent corporate organ.

### **Review of Literature**

There is vast literature on corporate governance. But there is very limited note on the duties and responsibilities of directors. The following are reviews:

According to Rehman<sup>2</sup>, an organization or company board of directors who are appointed or elected by members should function to achieve organizational objectives. These organizational objectives are to be determined with duties, responsibilities and powers. The main responsibility of board is to include the number of other stakeholders, such as suppliers, employers and consumers in the business environment.

Robert Flannigan<sup>3</sup> in his study on corporate boards discusses at length about the fiduciary duties through which boards are accountable. He discusses on the difficulties of the board to

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<sup>2</sup> Rehman, Abdul, (2013). Roles, Responsibilities and Functions of Board of Directors in an Organization, Available at SSRN: <http://ssrn.com/abstract=2276831> or <http://dx.doi.org/10.2139/ssrn.2276831>

<sup>3</sup> Flannigan Robert, (2004). Fiduciary Duties of Shareholders and Directors, the Journal of Business Law; Sweet & Maxwell and Contributors, May 2004 issue

understand the functions of fiduciary jurisdiction. These have been designed to supervise how shareholders behave, how directors manage the affairs of the corporation, etc. rather, not to operates towards general civil liability of discussing the discipline, self-interested conduct, limited access arrangements, etc. He further suggests that the conventional function requires either reaffirmation, or explicit reformation.

Adrian Fong<sup>4</sup>, in his study titled ‘Roles and responsibilities of 21<sup>st</sup> Century’ briefly notes the historical and legal framework of the board, explores contemporary issues and responsibilities regarding corporate governance, and then considers the future direction of the responsibilities of board. The study was focused on Hong Kong boards. The study concluded that Hong Kong Boards should have clear and comprehensive framework of roles and responsibilities to meet the challenges of the 21<sup>st</sup> century. Observing existing problems, this study also seeks to recommend best practices which will enable the boards to practice corporate governance more effectively. The study further highlighted the responsibilities of the board regarding corporate governance can be divided as monitoring and oversight of the company, accountability to shareholders, board evaluations and nominating directors and senior management.

Ernest Lim<sup>5</sup> discusses the new framework of the duties of directors before the enactment of the Companies Act 2006. The equitable principles on directors’ fiduciary duties of loyalty comprising the no-conflict and no-profit rules have been characterized in the form of either

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<sup>4</sup> Fong, Adrian, (2012). Roles and Responsibilities of 21st Century Board (October 25,). Available at SSRN:<http://ssrn.com/abstract=2166786> or <http://dx.doi.org/10.2139/ssrn.2166786>

<sup>5</sup> Lim, Ernest, (2013). *Directors' Fiduciary Duties: A New Analytical Framework*, Law Quarterly Review 129 (242). Available at SSRN: <http://ssrn.com/abstract=2368147>

a strict or flexible approach. The rules are said to be inexorable and inflexible. It is irrelevant whether the company could or would exploit the opportunity, whether the director has acted in good faith or whether the third party refuses to deal with the company.

Martin Gelter identifies the fundamental contradiction in the law of fiduciary duty of corporate directors across jurisdictions, namely the tension between the uniformity of directors' duties and the heterogeneity of directors. The selection criteria of the directors are often formal or informal. In many cases, the law facilitates the nomination. Legal rules tend nevertheless to treat directors as homogeneous groups that are expected to pursue a uniform goal. The questions relating to why do jurisdictions require employee representation to strongly advocate employee interest? The study explores the various situations in the countries of US, UK, German and France. The chapter further discusses and explores tension from the perspective of economic and behavioral theory.<sup>6</sup>

Prof. April (2000)<sup>7</sup> studied 687 large, publicly-traded U.S. firms between 1992 and 1993 to study the impact of Audit Committee and Board of Director Characteristics on Earnings Management of companies. Based on the study, she suggested that a non-linear negative relationship is found between audit committee independence and earnings management. But earnings management is positively related to whether the CEO sits on the board's compensation committee. And earnings management is negatively related to (a) CEO

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<sup>6</sup> Gelter, Martin and Helleringer, Geneviève, (2013). *Constituency Directors and Corporate Fiduciary Duties*, Forthcoming: The Philosophical Foundations of Fiduciary Law (Andrew Gold & Paul Miller eds., Oxford University Press, 2014); Fordham Law Legal Studies Research Paper No. 2341660. Available at SSRN:<http://ssrn.com/abstract=2341660> or <http://dx.doi.org/10.2139/ssrn.2341660>

<sup>7</sup> Klein, April (2000). Causes and Consequences of Variations in Audit Committee Composition. New York University Center for Law and Business, Working Paper No. 00-002

shareholdings, (b) Whether a large outside shareholder/director sits on the board's audit committee. The author concludes, "This paper lends support to the exchanges' and SEC's assertions that for all trading companies, investors will be best served if their elected boards provide corporate governance mechanisms consistent with achieving unbiased, transparent financial statements."

Anderson, Ronald C. Bizjak, John M (2000)<sup>8</sup>, made an attempt to understand the role of CEO in Structuring Executive Pay. They studied a random sample of 75 New York Stock Exchange firms, between 1985-94 and suggests that no convincing evidence is found that shows the presence of the CEO on the compensation committee, in terms of pay structure, is problematic for shareholders. . .' but "Because of their high levels of ownership, the sensitivity of total wealth (options and stockholdings) to firm performance is greater for CEOs that sit on their own compensation committees." Forcing the CEO off the compensation committee may also motivate CEOs to sell equity. Taking away flexibility in board design and contracting may result in suboptimal contracts and behavior and impose contracting costs on the firm.

Bhagat, Sanjai Carey, Dennis Elson, Charles (1999)<sup>9</sup> studied to understand the Director Ownership, Corporate Performance and Management Turnover in 449 companies in the US. From the results he suggested that, there was a significant correlation between the amount of stock owned by individual outside directors and firm performance. Second, and more

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<sup>8</sup> Anderson, R. C. and J. M. Buzjak, 2000. An empirical examination of the role of the CEO and the compensation committee in structuring executive pay. Working Paper American University.

<sup>9</sup> Bhagat, Sanjai, Dennis Carey and Charles Elson, 1999, Director ownership, corporate performance, and management turnover," *The Business Lawyer* 54, 885-919

important for the analysis, the greater the dollar value of the individual outside director's equity-holdings in the enterprise, the more likely a disciplinary-type CEO turnover in a poorly performing company would exist." Yermack, David (1996)<sup>10</sup>, studied 452 large U.S. industrial corporations between 1984 and 1991 to understand the impact of board size and board compensation on Market Valuation of Companies. He found an inverse association between board size and firm value. Companies with small boards also exhibit more favorable values for financial ratios, and provide stronger CEO performance incentives from compensation and the threat of dismissal. He concludes that number of directors is but one of many board attributes that might contribute to firm value, and that the complex associations between board size and other variables do not suggest clearly whether firms with small boards should have high or low market values.

Klein, April (1998)<sup>11</sup>, studied the effectiveness of affiliated directors (non-independent directors). Strong associations are found between the specific economic needs of companies and the incidence of directors most likely to fulfill these needs. It suggests that affiliated directors are effective directors. In fact, the results suggest that firms place affiliated directors on their boards to serve the specific, strategic needs of firms.

Jayesh Kumar (2005), studied the influence of Corporate Governance Mechanisms on Firm Financing in India. This study investigates the firm financing patterns in India and the role of corporate governance mechanisms and duties of directors. He used firm-level time series data of nearly 2000 listed companies from 1994 through 2000, to analyze the firm's

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<sup>10</sup> Yermack, David, 1996, Higher market valuation for firms with a small board of directors, *Journal of Financial Economics* 40, 185-211

<sup>11</sup> Klein, April, (1998). Firm performance and board committee structure, *The Journal of Law and Economics*, Vol. 41, No. 1, pp. 275-304

corporate financing behavior in connection with its corporate governance arrangements, specially its shareholding pattern. Results show that the capital structure of the firm is non-linearly linked to its corporate governance mechanisms (ownership structure); the firms with weaker corporate governance mechanisms (dispersed shareholding pattern, in particular measured by the entrenchment effects of group affiliation) tend to have a higher level of debt. Firms with higher foreign ownership or with low institutional ownership tend to have lower debt level. They do not find any significant relationship between ownership of directors and corporate with the firm financing in India. Overall, the findings presented in the paper provide evidence of definite role of corporate governance mechanisms in firm is financing decisions in India.

Globally companies are expected to do more than merely provide jobs and contribute to the economy through taxes and employment. Consumers and society in general expect more from the companies whose products they buy. This is coherent with believing the idea that whatever profit is generated is because of society, and hence mandates contributing a part of business to the less privileged. Further, separately in the light of recent corporate scandals, which reduced public trust of corporations, and reduced public confidence in the ability of regulatory bodies and organisations to control corporate excess. This has led to an increasing expectation that companies will be more open, more accountable and be prepared to report publicly on their performance in social and environmental arenas.

Businesses are recognizing that adopting an effective approach to CSR can open up new opportunities, and increasingly contribute to the corporates' ability to attract passionate and committed workforces.

### **Need of the Study**

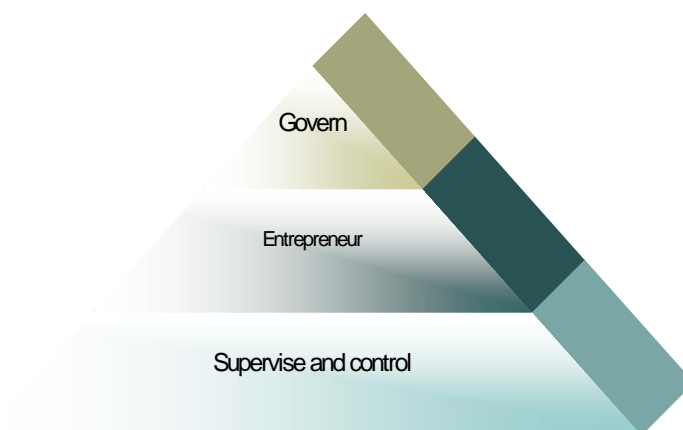
The objective of a company is to achieve long-term growth and sustainability. To this end, as representatives of the shareholders boards need to oversee the functioning of the organization and ensure that it continues to operate in the best interests of all stakeholders.

The roles of a Corporate Board of Directors are three fold.

- to Govern
- to Direct
- to Supervise and control

Figure 1.1 depicts the three fold roles of Boards of directors.

**Figure 1.1 : Role of Corporate Board of Directors**



The general duties and responsibilities of boards as below:

- The Board is responsible for governance i.e. ensuring the organization operates properly and effectively, and achieves its agreed objectives. Governance involves:
  - Setting a framework, system, procedures and policies that fulfils the objectives of the organization and needs of all stakeholders
  - Building the ethos and values that underpin the organization enabling and ensuring transparent and accountable decision-making
  - Compliance with the laws and regulatory environment
- The directors are responsible for giving strategic direction to the organization. This entrepreneurial role involves
  - Maintaining a long term overview of the organisation and all its work
  - Making strategic and major decisions towards achieving organizations objectives
  - Establishing operational policies and providing adequate resources for business activities
  - Appointing the CEO and management team and establishing management goals
- Finally the directors must constantly monitor the progress of the company towards its objectives as defined by shareholders. Supervising encompasses
  - Establishing control and accountability systems that enable risk to be assessed and managed
  - Monitoring use of firms' resources or wealth



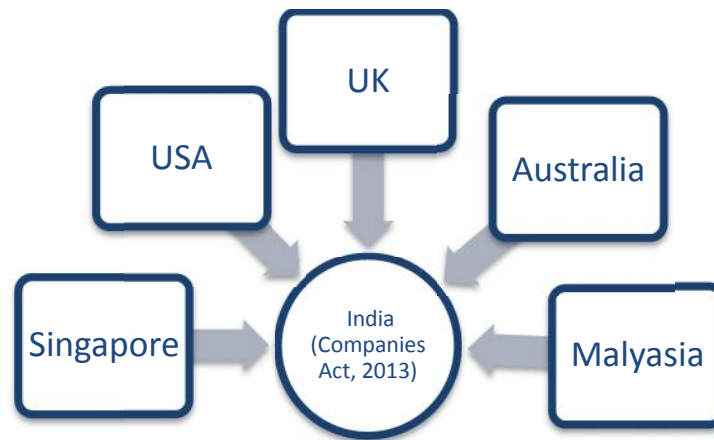
- Assessing progress of implementation of strategy
- Monitoring the management activities and achievement of the targets set
- Ensuring compliance with applicable laws and regulations

To fulfill their responsibility, the directors must understand their duties. Hence a set of duties for directors must be clearly laid down. The proposed study would try establish a connection between the existing duties in the countries referred. Further it makes a comparison of duties prevailing in India and countries abroad.

### **Research Design**

The study has been designed in two parts. First, the broad framework of corporate governance practices and secondly the duties laid down in the Acts. The study would compare the best practices with respect to the duties and responsibilities of boards and board committees of the selected countries. This would help to find gaps enabling Indian Corporates to review the existing process and benchmark with global standards.

### **Figure 1.2 : Research Framework**



### **Research Objective and Methodology**

The main objectives of the study are to:

- understand corporate governance practices and codes of countries under reference
- list down the various provision that are existing in the Companies Act with respect to the duties and responsibilities of boards and board committees of countries under reference
- compare the legal frameworks with respect to the duties and responsibilities of boards and board committees
- highlight the case studies of the companies with respect to the duties and responsibilities of boards and board committees

### **Methodology**

The primary sources include the information on stock exchanges, listing agreements, interactions with stakeholders, etc and secondary sources includes annual reports, committee reports, etc. The study has used research methods such as interviews, observations and documentary analysis. The interviews were conducted with experts from India and abroad.

Documentary analysis was the main source of data analysis. Both the primary and secondary data has been used for the study.

### **Chapterization**

The chapterization for the study is as follows:

Chapter 1: Duties of Board and Board Committees

Chapter 2: Corporate Governance: An Overview

Chapter 3: Corporate Governance in India

Chapter 4: Corporate Governance: International Perspective

Chapter 5: Duties of Directors: A Comparative Analysis

## Chapter 2 : Corporate Governance : An Overview

*The chapter discusses the broad framework of corporate governance, meaning and definition, need of corporate governance, corporate governance and state owned enterprises, and models of corporate governance*

### **Prelude**

In recent years, there has been an increasing focus on corporate governance (CG), particularly after the Global Financial Crisis (GFC). Many countries and jurisdictions have updated their corporate governance codes. The concept of CG has grown due to the massive corporate failures characterized decade of the twenty first century, the burst of the dot.com bubble in 2000 to malfeasance at Enron, Tycon, Worldcom, etc resulting to global corporate crisis at international level. This has resulted in unrest among the investors, regulators, politicians, stock exchanges, etc. In light of the global failure cases, countries around the world have responded by enacting the governance framework for protecting the interests of stakeholders. USA was first to initiate the regulation by issuing Sarbanes Oxley Act in July 2002. Thus the concept of Corporate Governance has come to limelight as an issue ever since people began to organize themselves for a common purpose. But still, good corporate governance practices cannot be legislated. This does not mean that the legal framework is not important. Legislation prescribes the minimum. The responsibility lies on the how the boards are built, their legal framework to raise standards beyond compliance, where the spirit of best practices adapted, their intent are fully embraced, ethical code of conduct, etc. The board is responsible for internal culture that promotes good corporate governance at

workplace. Boards need to recognize that good corporate governance culture adds value to the company. They can no longer be reactive, dependent and accommodating, as there are pressures on boards to accomplish more in a shorter time and in the right way. In this regard, the overall objective of the board is to move away from their role as mere advisers and to become active in terms of fiduciary responsibilities. A culture of good governance in the boardroom therefore needs to be inculcated as much as the rules themselves and this requires education and persuasion.

### **Meaning and Definition**

Corporate Governance is a *legal discipline*. The term ‘governance’ derives from the Latin ‘gubernare’ meaning to ‘to steer’, applying the meaning to steering of a ship. In general, CG deals with the structure and functioning of the boards of directors and their relationship with management in delivering the corporate objectives.

Cadbury Committee, 1992 defines Corporate Governance as:

*“the system by which companies are directed and controlled”.*

The OECD defines Corporate Governance as :

*"Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined."*

The significance of CG for stability and equity of society is captured by Adrian Cadbury as

*“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 require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interest of individual's corporations and society".*

The ongoing nature of CG indicates by the definition of the commission of Global Governance as *"a continuing process through which conflicting or diverse interest may be accommodated and co-operative action may be taken"*

*According to Mr Lim<sup>12</sup>, Corporate Governance is an ongoing process, so continuous review is necessary. Too often we adopt measures that are used in other countries. As long as we need money from these other markets, we need to play to their music. However, we should be more concerned about achieving compliance with the rules that we have put in place. We should not put in new rules just for the sake of putting them in"*

#### **Meaning : Corporate Governance**

*"The framework of rules, relationships, systems and processes within and by which authority is exercised and controlled in corporations."*

#### **Need for Corporate Governance**

The global business need to access global pools of capital, need to attract and retain the best human capital from world, collaborate with global corporate communities, etc. To achieve this, they need to demonstrate ethical codes in the business in-terms of values, principles, code of conduct, transparency, reporting mechanisms, regularizing core operations, leadership, stakeholder involvement, etc. Corporate entities need to recognize that their growth requires the cooperation of all the stakeholders to enhance the best corporate

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<sup>12</sup> Mr John Lim, Chairman, Singapore Institute of Directors

governance practices. In this regard the management needs to act as a trustee of the shareholders at large and prevent asymmetry of benefits between various sections of the shareholders, especially between the owners – managers – shareholders. Corporate governance is a key element in improving the economic efficiency of a firm. Good corporate governance helps to ensure the stakeholders interest, in general, and shareholders, interest in particular.

### **Why is Good Corporate Governance Important?**

Policy makers, practitioners and theorists have adopted the general stance that corporate governance reform is worth pursuing, supporting such initiatives as splitting the role of chairman / chief executive, introducing non-executive directors to boards, curbing excessive executive performance-related remuneration, improving institutional investor relations, increasing the quality and quantity of corporate disclosure, inter alia. However, is there really evidence to support these initiatives? Do they really improve the effectiveness of corporations and their accountability? There are certainly those who are opposed to the ongoing process of corporate governance reform. Many company directors oppose the loss of individual decision-making power, which comes from the presence of non-executive directors and independent directors on their boards. They refute the growing pressure to communicate their strategies and policies to their primary institutional investors. They consider that the many initiatives aimed at 'improving' corporate governance in UK have simply slowed down decision-making and added an unnecessary level of the bureaucracy and red tape (refer to summary Richard Branszn's experiment with the stock market). The

Cadbury Report emphasized the importance of avoiding excessive control and recognized that no system of control can completely eliminate the risk of fraud (as in the case of Maxwell) without hindering companies' ability to compete in a free market (Cadbury Report, 1992, p. 12, para 1.9). This is an important point, because human nature cannot be altered through regulation, checks and balances. Nevertheless, there is growing perception in the financial markets that good corporate governance is associated with prosperous companies. The research of Solomon J. and Solomon A. showed some evidence to support the agenda for corporate governance reform. The findings indicated that the institutional investment community considered both company directors and institutional investors welcomed corporate governance reform, viewing the reform process as a 'help rather than a hindrance'. Specifically, towards corporate governance reforms (Solomon J. and Solomon A., 1999)

### **Parties to Corporate Governance**

Parties involved in corporate governance include the regulatory body (e.g., the Chief - Executive Officer, the board of directors, management and shareholders). Other stakeholders who take part include suppliers, employees, creditors, customers and the community at large. In corporations, the shareholder delegates decision rights to the manager to act in the principal's best interests. This separation of ownership firm control implies a loss of effective control by shareholders over managerial decisions. Partly as a result of this separation between the two parties, a system of corporate governance controls are implemented to assist in aligning the incentives of managers with those of shareholders.



With the significant increase in equity holdings of investors, there has been an opportunity for a reversal of the separation of ownership and control problems because ownership is not so diffuse. A board of directors often plays a key role in corporate governance. It is their responsibility to endorse the organization's strategy, develop directional policy, appoint, supervise and remunerate senior executives and to ensure accountability of the organization to its owners and authorities. The effective performance of the organization depends on direct or indirect interest of various parties involved in CG. Directors, workers and management receive salaries, benefits and reputation, while shareholders receive capital return. Customers receive goods and services; suppliers receive compensation for their goods or services. In return these individuals provide value in the form of natural, human, social and other forms of capital. A key factor in an individual's decision to participate in an organization, e.g., through providing financial capital and trust that they will receive a fair share of the organizational returns. If some parties are receiving more than their fair return then participants may choose not to continue participating leading to organizational collapse.

### **Corporate Governance and State Owned Enterprises (SOEs)**

Corporate governance in State Owned Enterprises / Public Enterprises is a new phenomenon. In its ambit, the responsibilities of an enterprise to its customers, employees, society/government, suppliers and creditors are defined and a stock taking is done at the end of a specified period to ensure whether such responsibilities have been fulfilled or not. The

board of directors of the enterprise has to assume the responsibility of installing the systems of corporate governance in the enterprise and overseeing its effective implementation.

A number of enterprises have been taken by surprise by the process adopted by the government of liberating the Indian Economy from the shackles of controls, quotas, embargoes and protection. Many public enterprises have turned sick, as their products have no appeal left for consumer.

PE boards have been an utter failure with regard to succession planning. No effort is made to groom people internally to succeed the CEO. Sometimes, PE boards just do not have an idea as to who could succeed the CEO in the event of his retirement or resignation, as they have had no time to observe the style and functioning of their immediate junior colleagues. Most boards do not even recommend the names of insiders to their administrative ministry or to the Public Enterprise Selection Board (PESB) nor lobby the case of the insiders.

**Table 2.1 : Comparison of Agency Theory and Stewardship Theory**

<b>S.No</b>	<b>Criteria</b>	<b>Agency Theory</b>	<b>Stewardship Theory</b>
1	Model of Man	Economic Man	Self-Actualized Man
2	Behavior	Self-Serving	Collective Serving
3	Motivation	Lower order/economic needs (Physiological, security, economic)	Higher order needs (growth achievement, self-actualization)
4	Social Comparison	Other Managers	Principal
5	Identification	Low value commitment	High value commitment
6	Power	Institutional (legitimate, coercive,	Personal (expert,

		reward)	referent)
7	Management Philosophy	Control oriented	Involvement oriented
8	Risk Oriented	Control mechanisms	Trust
9	Time Frame	Short-term	Long-term
10	Objective	Cost Control	Performance enhancement
11	Cultural difference	Individualism	Collectivism
		Higher power distance	Low power distance

### **Theory of Corporate Governance**

The unique characteristics and distinctive features of four important models of corporate governance are detailed below:

- The Anglo-American Model
- The German Model
- The Japanese Model
- The Indian Perspective

#### **The Anglo-American Model**

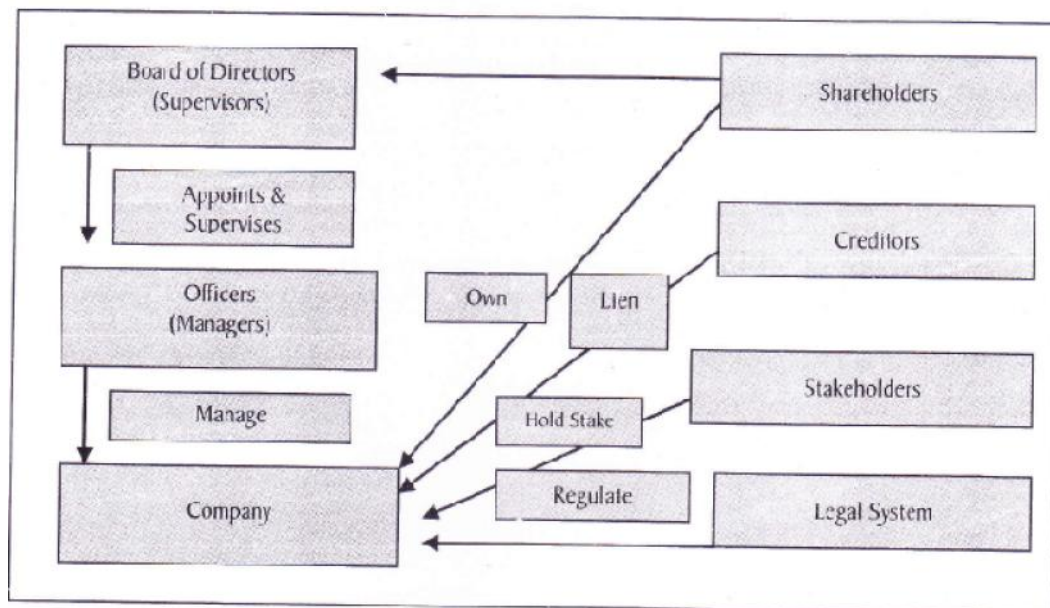
In this model, the board appoints and supervises the managers who manage the day-to-day affairs of the corporation. While the legal system provides the structural framework, the stakeholders in the company will be suppliers, employees and creditors. However, creditors exercise their lien over the assets of the company. The policies are framed by the board of directors and implemented by the management. The board oversees the implementation

through a well-designed information system. The board of directors, being responsible to their appointers - the shareholders - commits to them certain returns within the board contours of the market framework.

The distinctive features are:

- i. Clear separation of ownership and management, which minimizes conflict of interests.
- ii. Companies are run by professional managers who have negligible ownership stakes linked to performance. CEO has a major role to play.

**Figure 2.1 : The Anglo-American Model**



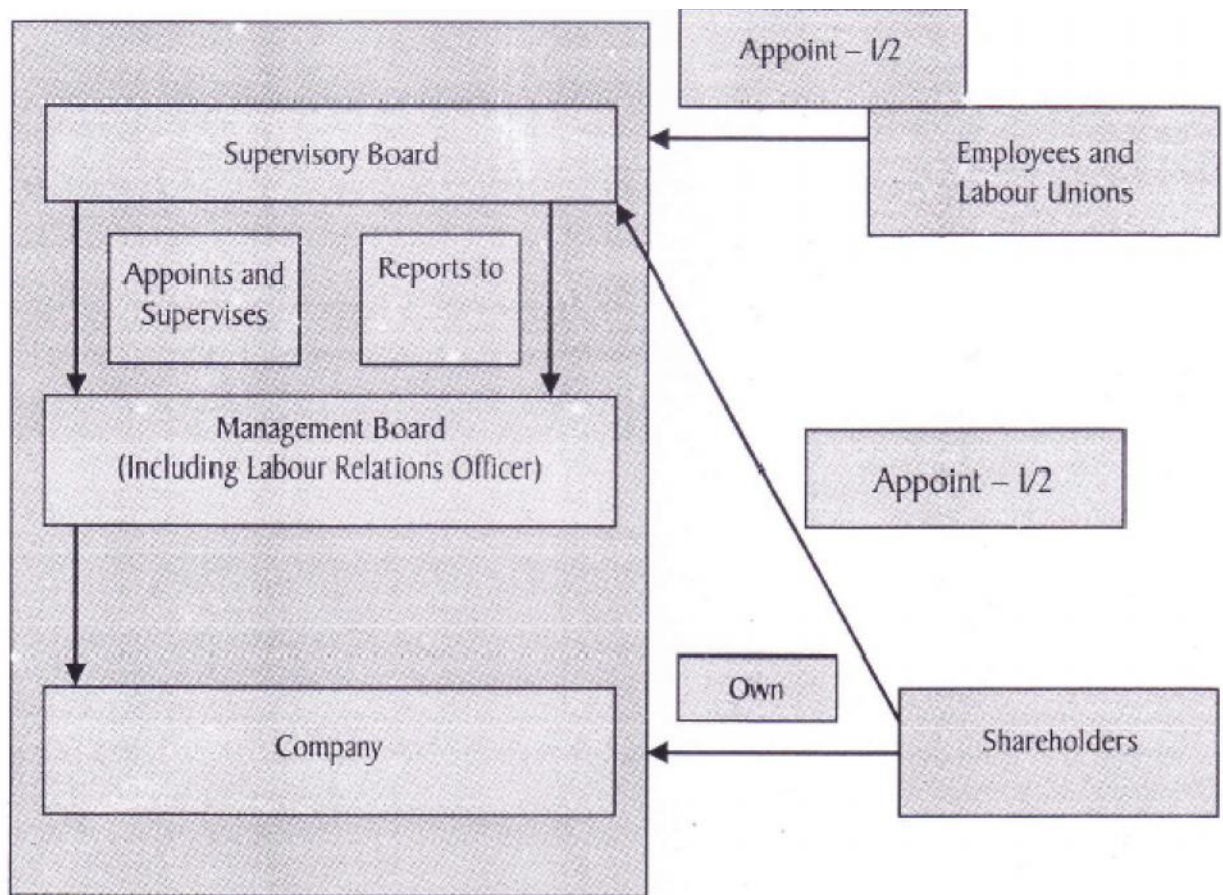
### **The German Model**

In this model, although the shareholders own the company, they do not entirely dictate the governance mechanism. As shown, shareholders elect 50 per cent of members of supervisory board and the other half is appointed by labour unions. This ensures that employees and laborers also enjoy a share in the governance. The supervisory board appoints and monitors the management board. There is a reporting relationship between them, although the management board independently conducts the day-to-day operations of the company.

The distinctive features are:

- i. Banks and financial institutions have substantial stake in equity capital of companies.
- ii. Labour Relations Officer is represented in the management board. Worker participation in management is practiced.
- iii. Both shareholders and employees have equal say in selecting the members of the supervisory board.

**Figure 2.2 : The German Model**



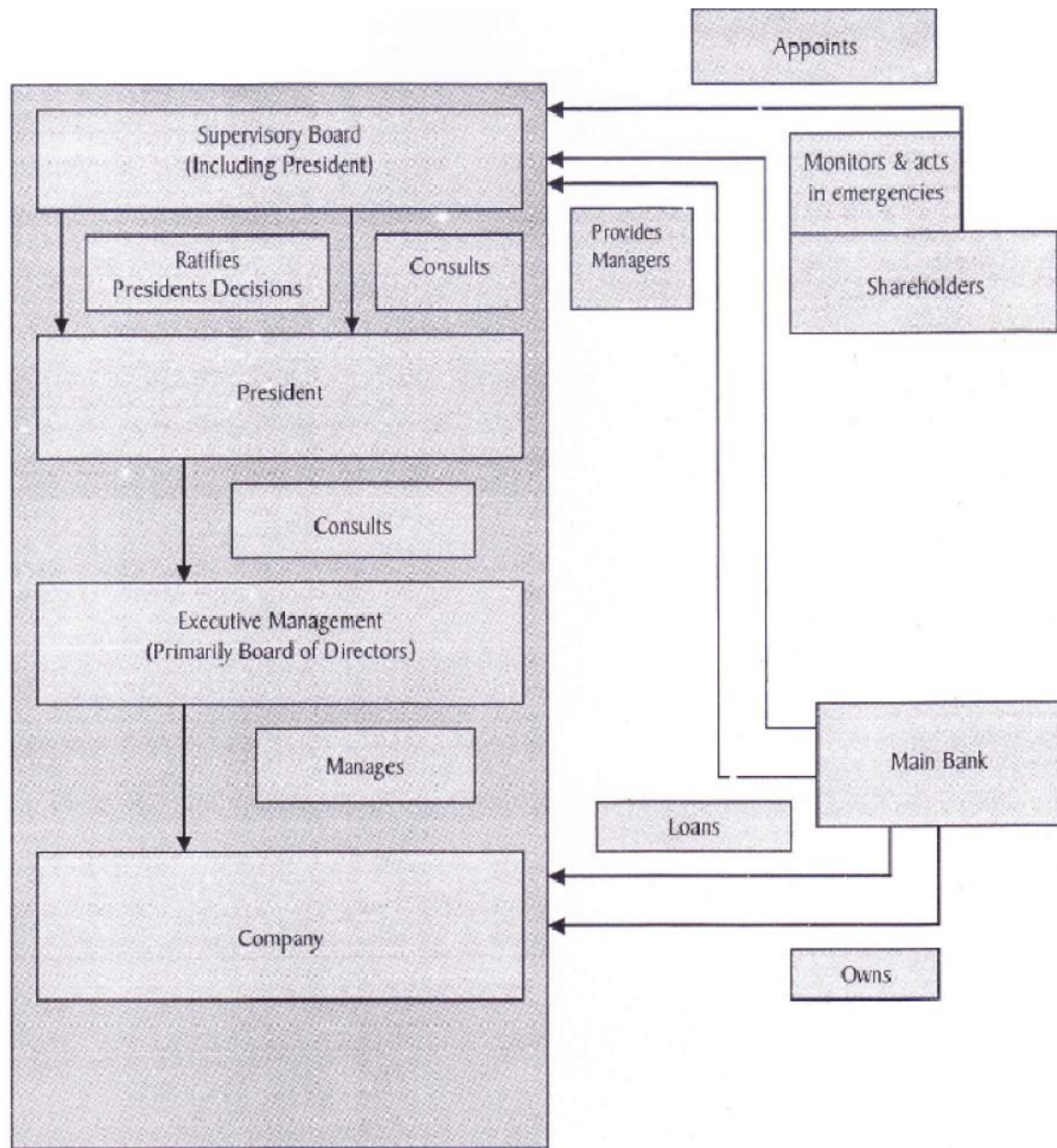
### **The Japanese Model**

In Japanese model, the financial institution has accrual role in-governance. The shareholders and the bank together appoint board of directors and the president.

The distinctive features are:

- i. Inclusion of President who consults both the supervisory board and the executive management.
- ii. Importance of the lending bank is highlighted

**Figure 2.3: The Japanese Model**



### **The Indian Perspective (Governance in the Public Sector)**

India in its own right has a unique and epochal background of governance. In the ancient times, the King was always considered the representative of the people. The wealth of the State was not the personal wealth of the king. Various modern authors have also taken tips

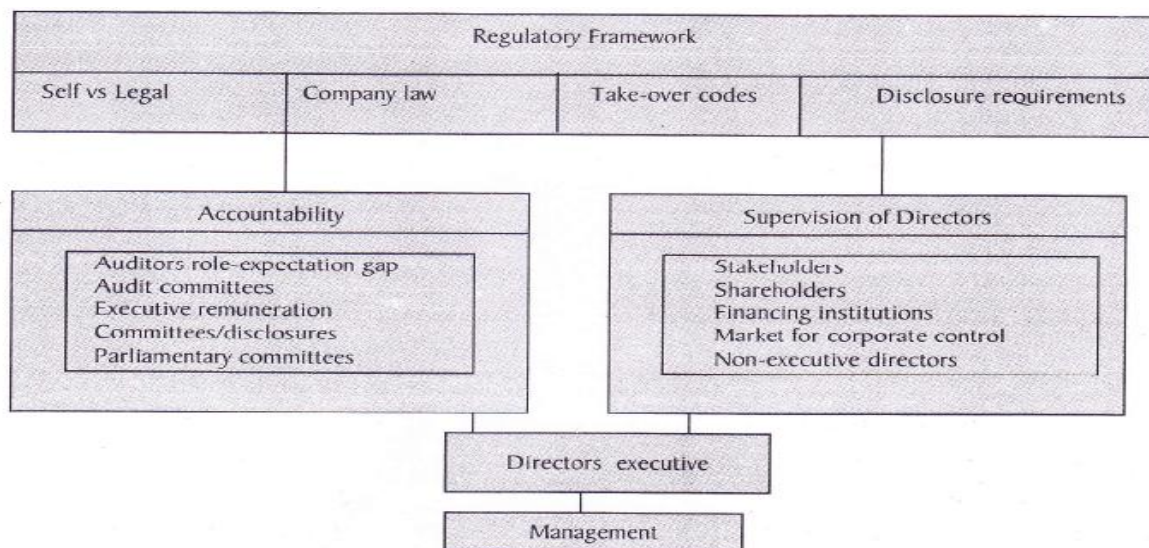


on good governance from Kautilya's Arthashastra. The earlier Indian corporates are governed by the Company's Act of 1956 that followed the UK model. The pattern of private companies is mostly that of closely held or dominated by a founder, his family and associates. In respect of public enterprises, central/state government forms the board. The hold of the government constitutes is to be dominant.

The distinctive features are:

- i. Equity shares are owned wholly or substantially (51 percent or more) by the government.
- ii. Good deal of political and bureaucratic influence over the management.
- iii. Organization often viewed as a social entity.
- iv. The boards of directors are appointed by the controlling administrative ministry.
- v. Excessive emphasis on observing rules, regulations and guidelines.
- vi. Efficiency and performance are sacrificed at the altar of propriety.

**Figure 2.4: The Indian Perspective of Corporate Governance**





## Committees on CG

The various committees that were formed to intensify the practices of the corporate governance are depicted in the following table 2.2 The Cadbury Committee was the first committee to be constituted to report on the financial aspects of corporate governance during 1992. The report was compiled on the basic assumption that the existing, implicit system of CG in UK.

**Table 2.2 : Summary of the Committees**

S.No	Committees	Year	Purpose	Focus
1	Cadbury	1992	The Cadbury committee was the first committee to be constituted to report on the financial aspects of corporate governance	The Cadbury Report focused attention on the board of directors as being the most important corporate governance mechanisms, requiring constant monitoring and assessment. However, the accounting and auditing function were also shown to play an essential role in good corporate governance, emphasizing the importance of the corporate transparency and communication with shareholders and other shareholders.
2	Greenbury	1995	Remuneration of Directors	The Greenbury Committee were keen to ensure that directors' remuneration was

				linked to company performance, and the committee did not seem to see a problem with high levels of pay per se, as long as they were justified on the basis of the company's financial results.
3	Hampel	1998	To review implementation of the findings of the Cadbury and Greenbury Committees.	The Hampel Report emphasized the need to maintain principles-based, voluntary approach to corporate governance rather than a more regulated and possibly superficial approach.
4	Turnbull	1999	The Turnbull Committee was established specifically to address the issue of internal control and to respond to these provisions in the combined code.	The aim was to provide companies with general guidance on how to develop and maintain their internal control systems and not to specify the details of such a system.
5	Higgs	2003	The Higgs Report dealt specifically with the role and effectiveness on non-executive directors, making recommendations for changes to the Combined	The general recommendations included a greater proportion of non-executive directors on boards (at least half of the board) and more apt remuneration for non-executive directors.

			Code.	
6	Smith	2003	In response to the Enron scandal Commissioned this committee, inter alia, with the aim of examining the role of audit committee in UK corporate governance	The main issue is dealt within the report concerned the relationship between the external auditor and the companies they audit, as well as the role and responsibilities of companies' audit committees.
7	Sarbanes-Oxley Act	2002	In the USA, corporate crisis associated with companies such as Enron, Tyco and Global Crossing seem to have hastened the introduction of the Sarbanes-Oxley legislation. There is some evidence that the bankruptcy of WorldCom on 21 July, 2002, and the public outrage that followed, encouraged President G.W. Bush to sign into law nine days later the Sarbanes-Oxley legislation	The Sarbanes-Oxley Act introduced sweeping corporate law changes relating to financial reporting, internal accounting controls, and personal loans from companies to their directors, whistle blowing and destruction of documents. In addition, Sarbanes-Oxley severely restricts the range of additional services that an audit firm can provide to a client.

### **Chapter 3 : Corporate Governance in India**

*The present chapter outlines the CG framework in India. The chapter discusses at length meaning of corporate governance, role of regulators, committees, legal frame, Companies Act, autonomy and responsibilities of CPSEs, duties of board and board committees in India.*

#### **Introduction**

The essence of corporate governance lies in promoting and maintaining integrity, transparency and accountability in the highest echelons of management. The term corporate governance is sometimes used very widely embracing a company's relations with a wide range of stakeholders comprising shareholders, managers, employees, customers, suppliers, labour unions, providers of finance, regulators and the community at large or very narrowly referring to a company's compliance with the provisions of best practice codes. It is the boarder approach of corporate governance that is more meaningful in achieving sustainability.

Indian regulatory framework of corporate governance started way back during 1988 with the establishment of SEBI. During 1992, SEBI became fully autonomous to regulate the Indian capital markets. The main function of SEBI is to maintain stable and efficient markets by creating and enforcing regulations in the market place. During 1998, India produced the first substantial code of best practices on corporate governance after the start of the Asian Financial Crises in mid 1997. Confederation of Indian Industry began to work on the CII

Code of Corporate Governance, 1998. Kumara Mangalam Birla was appointed as the Chairman to work on the revised code of the CII during 1999. The new National Code on Corporate Governance was released during 2000 and was approved by SEBI. Later SEBI revised its Listing Agreement to incorporate the recommendation of the country's new code on corporate governance. The rules contained a section Clause 49 of the Listing Agreement took effect in phases over 2000 – 2003. SEBI mandated that listed companies to comply with the corporate governance related provisions of the Clause 49 of the Listing Agreement. The New Companies Act, 2013 has been enacted with 470 Sections, 29 Chapters, 7 schedules. The duties of directors have been laid down in Section 166 of the Indian Companies Act 2013. Efficient corporate governance requires clear understanding of the respective roles of boards and senior management and their relationships with others in corporate structure. The relationships of the Board and management shall be characterized by sincerity; their relationships with employees shall be characterized by fairness, their relationships with government shall be characterized by commitment to compliance. The board of directors has the important role of overseeing management performance on behalf of the company.

#### **Clause 49 of the Listing Agreement**

As per Clause 49 of the Listing agreement of the SEBI, the companies agree to comply on the following provision:

##### ***Composition of Board***

- The Board of directors of the company shall have an optimum combination of executive and non-executive directors with not less than fifty percent of the board of directors comprising of non-executive directors.
- Where the Chairman of the Board is a non-executive director, at least one-third of the Board should comprise of independent directors and in case he is an executive director, at least half of the Board should comprise of independent directors.

Provided that where the non-executive Chairman is a promoter of the company or is related to any promoter or person occupying management positions at the Board level or at one level below the Board, at least one-half of the Board of the company shall consist of independent directors.

Every Company to have a board of directors consisting of individual director with Minimum Directors as follows:

- Public companies: 3 directors
- Private companies: 2 directors
- One person company: 1 director

Maximum directors: 15 (except with special resolution). In the New Companies Act, 2013 it has been mandated have to have at least one woman for the listed companies.

### **Code of Conduct**

- i. The Board shall lay down a code of conduct for all Board members and senior management of the company. The code of conduct shall be posted on the website of the company.
- ii. All Board members and senior management personnel shall affirm compliance with the code on an annual basis. The Annual Report of the company shall contain a declaration to this effect signed by the CEO.

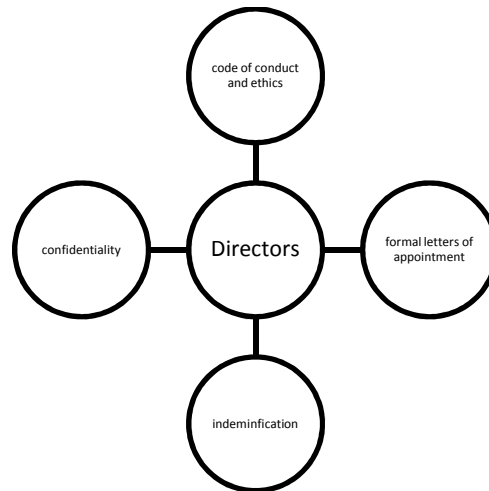
### **Board Responsibilities**

The board of director's of the company represents the shareholders interest in perpetuating a successful business and optimizing long-term financial returns in a manner consistent with applicable legal requirements and ethical considerations. The Board is responsible for identifying and taking reasonable actions to held and assure that the Company is managed in a way designed to achieve this results.

### **Duties of Directors**

The basic responsibility of the Directors is to exercise their business to act in reasonably responsible manner in the best interests of the Company and its shareholders. In discharging these obligations, directors shall rely on the honesty and integrity of the executives, customers, advisors and auditors. The Directors shall acknowledge and sign the following documents:

### **Figure 3.1 : Mandated documents for Directors**



The specific duties of the Board of Director's are as follows:

- Director shall act according to articles of company , subject to act
- Director of company shall act in good faith in interest of company and its stakeholders
- Shall exercise duties with due and reasonable care, skill diligence and independent judgment
- Director should not involve in a situation where his interest may conflict the interest of the company.
- Director should not try for any undue gains from the company and in case found guilty, shall be liable to pay an amount equal to that gain to the company.
- Director of a company shall not assign his office and any assignment so made shall be void.
- In case of contravention, director shall be punished with a fine of not less than Rs. 1 lakh, but which may extend to Rs.5 lakh



### **Powers of Board as per Companies Act, 2013**

- The Board of Directors are entitled to exercise all such powers or do such acts as a company has, subject to this Act, memorandum and articles of the company and any other regulation including regulations made in general meeting and any power to be exercised in a general meeting
- Regulation made by the company in general meeting shall not invalidate any prior act of Board, which would have been valid if the resolution had not been made.
- Board shall exercise following powers on behalf of the company by means of resolutions passed at its meeting:-
  - to call on share holders in case money unpaid on their shares
  - authorize buy-back of securities
  - issue securities, including debentures, whether in or outside India
  - to borrow monies
  - Invest funds of company
  - Grant loans or give guarantee or provide security in respect of loans
  - approve financial statement and Board's report
  - diversify the business
  - approve amalgamation, merger or reconstruction
  - take over a company or acquire controlling or substantial stake in a company
  - any other matter which may be prescribed.

For the purposes of section (k) of sub section (3) of section 179, the following powers of the Board of directors shall be exercised only by means of resolutions passed at meetings of the Board:

- to make political contributions;
- to fill a casual vacancy in the Board;
- to enter into a joint venture or technical or financial collaboration or any collaboration agreement;
- to commence a new business;
- to shift the location of a plant or factory or the registered office;
- to appoint or remove key managerial personnel (KMP) and senior management personnel one level below the KMP;
- to appoint internal auditors;
- to adopt common seal;
- to take note of the disclosure of director's interest and shareholding;
- to sell investments held by the company (other than trade investments), constituting five percent or more of the paid – up share capital and free reserves of the investee company;
- to accept public deposits and related matters and;
- to approve quarterly, half yearly and annual financial statements.

Boards are empowered delegate to any directors by passing a resolution in the meeting, the powers specified in section (d) to (f) on such conditions as the Board may prescribe.

## **Restrictions on Powers of Boards**

Board to exercise following powers only with the consent of the company by special resolution:-

- To sell, lease or otherwise dispose of whole or substantially the whole of the company or undertakings by the company
- To invest otherwise in trust securities, amount of compensation received as a result of merger or acquisition
- To borrow money in excess of its paid up capital and the free reserves.
- To remit or give time for repayment for any debt due from director
  - a. Every special resolution passed in general meeting in relation to the exercise of the powers to borrow shall specify total amount that may be borrowed by the Board of Directors.
  - b. Nothing shall affect the
    - i. title of buyer or person who buy or takes on lease any property, investment or undertaking as is referred to in good faith
    - ii. sale or lease of any property of the company where the ordinary business of the company consists of, or comprises such selling or leasing
  - c. Any special resolution passed by the company consenting to sell, lease or dispose of undertaking may stipulate conditions including the use, disposal or investment of the sale proceeds which may result from the transactions.

- d. No debt incurred by the company in excess of limit approved shall be valid or effectual, unless the lender proves that he advanced the loan in good faith.

### **Board Committees**

The following section discusses the duties of various board committees of which audit committee, nomination and remuneration committee, Risk management committee and CSR committee are mandated by the Companies Act 2013.

#### ***Audit Committees***

The audit committee shall have minimum three directors as members. Two-thirds of the members of audit committee shall be independent directors. All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise. The audit committee shall have powers, which should include the following:

- To investigate any activity within its terms of reference.
- To seek information from any employee.
- To obtain outside legal or other professional advice.
- To secure attendance of outsiders with relevant expertise, if it considers necessary.

The role of the audit committee shall include the following:

- Oversight of the company's financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct, sufficient and credible.

- Recommending to the Board, the appointment, re-appointment and, if required, the replacement or removal of the statutory auditor and the fixation of audit fees.
- Approval of payment to statutory auditors for any other services rendered by the statutory auditors.
- Reviewing, with the management, the annual financial statements before submission to the board for approval, with particular reference to:
  - Matters required to be included in the Director's Responsibility Statement to be included in the Board's report in terms of clause (2AA) of section 217 of the Companies Act, 1956
  - Changes, if any, in accounting policies and practices and reasons for the same
  - Major accounting entries involving estimates based on the exercise of judgment by management
  - Significant adjustments made in the financial statements arising out of audit findings
  - Compliance with listing and other legal requirements relating to financial statements
  - Disclosure of any related party transactions
  - Qualifications in the draft audit report
- Reviewing, with the management, the quarterly financial statements before submission to the board for approval
- Reviewing, with the management, the statement of uses / application of funds raised through an issue (public issue, rights issue, preferential issue, etc.), the statement of

funds utilized for purposes other than those stated in the offer document /prospectus/ notice and the report submitted by the monitoring agency monitoring the utilisation of proceeds of a public or rights issue, and making appropriate recommendations to the Board to take up steps in this matter.

- Reviewing, with the management, performance of statutory and internal auditors, adequacy of the internal control systems.
- Reviewing the adequacy of internal audit function, if any, including the structure of the internal audit department, staffing and seniority of the official heading the department, reporting structure coverage and frequency of internal audit.
- Discussion with internal auditors any significant findings and follow up there on.
- Reviewing the findings of any internal investigations by the internal auditors into matters where there is suspected fraud or irregularity or a failure of internal control systems of a material nature and reporting the matter to the board.
- Discussion with statutory auditors before the audit commences, about the nature and scope of audit as well as post-audit discussion to ascertain any area of concern.
- To look into the reasons for substantial defaults in the payment to the depositors, debenture holders, shareholders (in case of non payment of declared dividends) and creditors.
- To review the functioning of the Whistle Blower mechanism, in case the same is existing.

- Approval of appointment of CFO (i.e., the whole-time Finance Director or any other person heading the finance function or discharging that function) after assessing the qualifications, experience & background, etc. of the candidate.
- Carrying out any other function as is mentioned in the terms of reference of the Audit Committee.

### ***Nomination and Remuneration Committee***

Every board of listed company should constitute the Nomination and Remuneration Committee constituting 3 or more non-executive directors of which at least half should be independent directors. The chairman can be a member of the committee whereas, but not the chairman for the nomination and remuneration committee. The following are the duties of the Nomination and Remuneration Committee:

- Identify persons who may be appointed as directors and senior management, and recommend to board appointment and removal of director and evaluate performance of directors.
- Committee to formulated criteria for determining qualifications, attributes and independence of director and recommend to board policy regarding remuneration of directors, key managerial personnel and other employees.
- While formulating policy committee should ensure following:-
  - Level and remuneration to directors should be sufficient to attract, retain & motivate directors of quality
  - Relationship of remuneration to performance is clear and meets appropriate performance benchmarks

- Remuneration to Directors and senior management involves a balance between fixed and incentives reflecting performance

### ***Stakeholders Relationship Committee***

Every company having more than 1000 (One thousand) Share Holders + Debenture Holders + Deposit Holders + Other Security Holders shall constitute a Stakeholders Relationship Committee, which shall consider & resolve the grievance of security holders. The committee comprises of a Chairperson and members would be nominated by the board.

### ***Corporate Social Responsibility Committee***

Companies having net worth of Rs. 500 crore or more, or turnover of Rs. 1000 crore or more or a net profit of Rs. 5 crore or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board.

Apart from these committees, Indian Listed enterprises are also following other committees as per there requirements. These includes Whistle Blower Committee, Executive Committee, Sexual Harassment and Redressal Committee, Project Management Committee, Health Safety Environment Committee, etc

### **Corporate Governance and Central Public Sector Enterprises (CPSEs)**

The importance of Corporate Governance principles in ensuring transparency and trust among the stakeholders was needed to adopt and apply the good Corporate Governance practices in respect of CPSEs March, 2010<sup>13</sup>. These Guidelines are applicable to CPSEs and cover issues like composition of Board of CPSEs, Audit Committee, Remuneration

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<sup>13</sup> Public Enterprise Survey, 2014-15, Department of Public Enterprise, MHI&PE, GoI



Committee, Subsidiary Companies, Disclosures, Code of Conduct and Ethics, Risk Management and Reporting, monitoring the compliance of Guidelines by the CPSEs and formation of Remuneration Committee.

The Board of Directors of a CPSE are delegated powers to follow the policy decisions issued by Government from time to time. The Government has granted enhanced powers to the Boards of Maharatna, Navratna, Miniratna and other profit making enterprises. The CPSEs following criteria are eligible to be considered a Maharatna CPSEs :

- Having Navratna status
- Listed on Indian stock exchange, with minimum prescribed public shareholding under SEBI regulations
- An average annual turnover during the last 3 years of more than Rs 25,000 crore
- An average annual net worth during the last 3 years of more than Rs 15,000 crore
- An average annual net profit after tax during the last 3 years of more than Rs 5,000 crore
- Significant global presence or international operations.

The Planning Commission of India had constituted a “Panel of Experts on Reforms in Central Public Sector Enterprises (CPSEs)” to examine a range of issues inter-alia relating to HR & Corporate Governance, MOU system, effective partnerships with private sector, diversifications, mergers & consolidation, technology mapping in the CPSEs and to suggest a road-map for further development<sup>14</sup>. The panel recommended a mandatory committee for

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<sup>14</sup> Roongta committee, 2011

CPSEs i.e Strategy and Business Development Committee. The main aim of the committee is to strategize and set direction for diversification, acquisition, joint venture, new business entity and to review existing organizational structure etc. Further; the committee recommended that there should be a separate role of nominee directors on the boards of CPSEs.

The board diversity dimension of CPSEs Boards in India has been discussed with reference to age, educational background, work experience and internationalization. Only the listed SOEs on the National Stock Exchange (NSE) have been considered for the study and compared with their counterparts in the private sector listed on the NSE. As the Table 3 shows of the total number of 42 listed SOEs in 2014, there were only 22 companies having 26 women directors on their boards. It may be noted that during 2012-13, 21 listed companies had a total number of 31 women directors on their Boards. For the non-SOEs listed on the NSE, this number increased from 533 in 2013 to 593 in 2014. The listed SOEs belonged to minerals, energy, financial services and steel sectors.

**Table 3.1: Listed SOE Boards in India**

<b>Particulars</b>	<b>2013</b>	<b>2014</b>
Total no. of Listed SOEs	42	42
SOEs having Women Board Members	21	22
Total no. of Women Board Members	31	26
Doctorates	8	5
Graduates	9	9

Post Graduates	14	12
No. of Women Directors in Listed Non-SOEs	533	593

The Section 149 of the Indian Companies Act, 2013 deals with the provisions relating to appointment of directors and matters such as the minimum and maximum number of directors, type / class of directors to be appointed. As per this Section:

- Every listed company shall appoint at least one woman director within one year from the commencement of the second provision to Section 149(1).
- Every other Public company: having paid up capital of 100 crore or more or a turnover of 300 crore or more have to compulsorily appoint within 3 years from the commencement of second proviso to Section 149(1) of the Act.

A time limit of one year is provided to fall in line with the new requirement. A search for right kind of women directors has to be made and it is certainly a time consuming exercise. As per section 152(5), every person including a woman director who has been appointed to hold the office of a director shall on or before the appointment furnish to the company consent in writing to act as such in Form No. 11.2 and comply with requirements for filing of consent on MCA portal. Woman director proposed to be appointed has to obtain DIN and shall give a declaration that she is not disqualified to be appointed as a director.

The presence of women directors on the boards of the listed SOEs very clearly points out that there has been little regard paid by the SOEs to the provisions of the Indian Companies Act 2013. About two-thirds of the women directors on the SOEs boards had doctorate or post graduate qualifications. They represented occupations such as civil services, consultancy, accounting, law and academia. Only one SOE had a women member as the Chairman and Managing Director.

## **Chapter 4 : Corporate Governance: International Perspective**

*The present chapter highlights the corporate governance practices in USA, UK, Australia, Singapore and Malaysia. The chapter discusses the existing legal framework, provisions, code of conduct, board and board committees, etc that are supporting the countries to strengthen their corporate governance structure.*

### **Corporate Governance in USA**

Corporate governance broadly refers to the mechanisms, processes and relations by which corporations are controlled and directed. Corporate governance includes the processes through which corporations' objectives are set and pursued in the context of the social, regulatory and market environment. Governance mechanisms include monitoring the actions, policies, practices, and decisions of corporations, their agents, and affected stakeholders. Governance structures and principles identify the distribution of rights and responsibilities among different participants in the corporation (such as the board of directors, managers, shareholders, creditors, auditors, regulators, and other stakeholders) and includes the rules and procedures for making decisions in corporate affairs. Corporate governance practices are affected by attempts to align the interests of stakeholders. Interest in the corporate governance practices of modern corporations, particularly in relation to accountability, increased following the high-profile collapses of a number of large corporations in the United States.

**Figure 4.1 : Historical Overview of Corporate Governance in USA**

**A Historical Overview of Corporate Governance in the USA**

	1960s-1970s	1980s	1990s	2000s
	Managerial Capitalism	Investor Capitalism	"Shareholder Value"	Crisis of "shareholder value" paradigm
Ownership	Dispersed, individual	Institutional investors	Institutional investors	Institutional investors
Market for Corporate Control	Weak	Strong	Medium	Medium
Boards	Insider - "advising board"	Insider- "advising board"	Outsider- "monitoring board"	Outsider- "monitoring board"
Executive Remuneration	Fixed	Stock options	Stock options	Stock options
Gatekeepers	Weakly regulated	Weakly regulated	Weakly regulated	Strongly regulated

(Source : Gregory Jackson, Understanding Corporate Governance in the United States An Historical and Theoretical Reassessment, pp 22)

### **Emergence of Corporate Governance**

There were several frauds and scams in the corporate history of the United States. The regulatory system was not satisfactory and needed an external regulation to control the frauds and scams. These regulations would penalize the wrong doers, while those who abide by rules be rewarded. There were several changes brought out by governments to protect the rights of shareholder, promoting large institutional investors, Corporates by adopting better governance practices. Further, supported in formation of several committees to study the issues in depth and make recommendations on the existing codes and guidelines on

Corporate Governance. All these measures have brought about a metamorphosis in corporate that realized that investors and society are serious about corporate governance system.

**Box 1 : Two major corporate scandals in the US**

***Waste Management Scandal (1998):*** A Houston-based publicly traded waste management company reported a \$1.7 billion in fake earnings. The major players for the scandal were Founder/CEO/Chairman Dean L. Buntrock and other top executives; Arthur Andersen Company (auditors). The company allegedly falsely increased the depreciation time length for their property, plant and equipment on the balance sheets. A new CEO and management team went through the books and identified the fraud. A class-action suit for \$457 million was filed and Securities Exchange Commission find Arthur Andersen with \$7 million penalty.

***Enron Scandal (2001) :*** A Houston-based commodities, energy and service corporation. The shareholders lost \$74 billion, thousands of employees and investors lost their retirement accounts, and many employees lost their jobs. The major players involved were CEO Jeff Skilling and former CEO Ken Lay. The CEO kept huge debts off the balance sheets. The internal employee Sherron Watkins identified the scam. The CEO was penalize and got 24 years imprisonment. The company filed for bankruptcy. Arthur Andersen was found guilty of fudging Enron's accounts.

The concept of CG gained importance with the occurrence of the Watergate scandal. Thereafter, as a result of subsequent investigations, US regulatory and legislative bodies

were able to find out failures that had allowed many corporations to make illegal, political contributions or to bribe government officials. This led to the development of the Foreign and Corrupt Practices Act (FCPA) of 1977 that contained specific provisions regarding the establishment, maintenance and review of systems of internal control. This was followed in 1979 by Securities and Exchange Commission's proposals for mandatory reporting on internal financial controls. In 1985, following a series of high profile business failures in the US, the most notable one of which being the savings and loan collapse, the Tradway Commission was formed to identify the main cause of misrepresentation in financial reports and to recommend ways of reducing incidence thereof. The Tradway Report published in 1987 highlighted the need for a proper control environment, independent audit committees and an objective internal audit function and called for published reports on the effectiveness of internal control. The commission also requested the sponsoring organizations to develop an integrated set of internal control criteria to enable companies to improve their control. The two scandals ie Enron and Worldcom has led to the debate over the performance of the corporate sector in the US. The Republican congress and President enacted the Sarbanes-Oxley Act of 2002. Sarbanes – Oxley Act in short is termed as SOX. SOX is generally seen as a piece of “progressive” regulation (Baker, 2008). The SOX reform changed the pattern of regulations, disclosure requirements mandating corporate governance. The Federal government has taken greater role, since the Stock Exchange Commission (SEC) has moved into areas that had been exclusively regulated. Finally, the role of largely self-regulated or professional groups such as accountants, auditors, analysts, middle managers, etc has been brought into the forefront of the corporate governance.



**Table 4.1 : Various committees /commissions / Act**

<b>Year</b>	<b>Name of the committees /commissions / Act</b>	<b>Remarks</b>
1933	Securities Act of 1933 (1933 Act)	Publicity-traded corporations must comply with federal securities laws
1934	Securities Exchange Act of 1934 (1934 Act)	
1977	Foreign and Corrupt Practices Act	Provisions regarding the establishment, maintenance and review of systems of internal control systems
1987	Tradway Report published in 1987	Proper control environment, independent audit committees and an objective internal audit function and insisted to publish reports on the effectiveness of internal control mechanisms
2002	Sarbanes-Oxley Act of 2002 (SOXA)	regulations, disclosure requirements mandating corporate governance

### **Corporate Governance Policy**

Corporate Law in the United States is composed of 50 states systems of corporate law. However there are additional sources of corporate law: the Model Business Corporation Act (hereafter referred to as the MBCA), which was drafted by the Section of Business Law of the American Bar Association (ABA), has been very influential on US corporate law and has so far been adopted by twenty four states.

The Model Business Corporation Act is not directly legally binding upon any corporation. The act must first be adopted by a state legislature before it has any legal effect. More than half of the states use some version of the Model Business Corporation Act. SOX act has important governance implications for listed corporations. SOX act applies to all SEC

registered organizations, irrespective of where their trading activities are geographically based. Under SOX, management is required to certify that the company's financial reports, by the management and accountant. SOX act is an serious attempt to portray the various issues associated with corporate failures and to achieve and restore investors confidence. The main aim of the SOX is to protect investor's interest by improving the disclosure norms, transparency in the transactions, regulating as per the legal provisions, etc. The important provisions in the SOX Act are briefly given below:

- Establishment of Public Company Accounting Oversight Board (PCAOB): SOX creates a new board consisting of five members of whom two will be certified public accountants. All accounting firms have to get registered with the board. The board will make regular inspection of firms. The board will report to SEC. The report will be ultimately forwarded to Congress.
- Audit Committee: The SOX provides for new improved audit committee. The committee is responsible for appointment, fixing fees and oversight of the work of independent auditors. The registered public accounting firms should report directly to audit committee on all critical accounting policies.
- Conflict of Interest: The public accounting firms should not perform any audit services for a publically traded company.
- Audit Partner Rotation: The act provides for mandatory rotation of lead audit or co-coordinating partner and the partner reviewing audit once every 5 years.

- Improper influence on conduct of Audits: According to act, it is unlawful for any executive or director of the firm to take any action to fraudulently influence, coerce or manipulate an audit.
- Prohibition of non-audit services: Under SOX Act, auditors are prohibited from providing non-audit services concurrently with audit financial review services.
- CEOs and CFOs are required to affirm the financials: CEOs and CFOs are required to certify the reports filed with the Securities and Exchange Commission (SEC).
- Loans to Directors: The act prohibits US and foreign companies with Securities traded within US from making or arranging from third parties any type of personal loan to directors.
- *Attorneys* : The attorneys dealing with publicly traded companies are required to report evidence of material violation of securities law or breach of fiduciary duty or similar violations by the company or any agent of the company to Chief Counsel or CEO and if CEO does not respond then to the audit committee or the Board of Directors.
- *Securities Analysts*: The SOX has provision under which brokers and dealers of securities should not retaliate or threaten to retaliate an analyst employed by broker or dealer for any adverse, negative or unfavorable research report on a public company. The act further provides for disclosure of conflict of interest by the securities analysts.

The most important aspect of SOX is that the senior officers are accountable and responsible for the corporate culture at the organizational level and stakeholders must have faith.

### **CG framework for SOEs**

US Corporate law provides for a 'single board system' with no compulsory labor representation. Each US Corporation must have a Board of Directors, except as provided in MBCA. Exceptions refer to a shareholders' agreement that may dispense with or limit the authority of the Board of Directors. In addition, US law provides for a shareholder's agreement as a tool to introduce a non-traditional corporate governance model. MBCA therefore requires that each corporation has a Board of Directors (except those with a shareholders' agreement and no other corporate bodies (supervisory etc.) are required in addition.

The powers and duties of the Board of Directors are defined by the following rule:

- All corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation managed by or under the direction of, its board of directors, subject to any limitation set forth in the articles of incorporation or in an agreement authorized.
- The Delaware code formulates the powers and duties in a way representative of all other US state corporate statutes, saying that 'the business and affairs of every corporation must be managed by or under the direction of a Board of Directors, except as may be otherwise provided in the code or in its certificate of incorporation'.<sup>15</sup>

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<sup>15</sup> Par. 141(a) of Delaware's incorporation law states that the business and affairs of every corporation have to be managed by or under the direction of a board of directors. However, it may be otherwise provided in its

- The Californian Corporation Code states that the Board may delegate the management of day-to-day operations to another person ‘provided that the business and affairs of the corporation shall be managed and all corporate powers shall be exercised under the ultimate direction of the board’. As described above, MBCA, section 8.01(a) requires that every corporation have a board of directors except that a shareholder agreement authorized by section 7.32 may dispense with or limit the authority of the board of directors (a nontraditional form of governance until the corporation becomes a public corporation). It also recognizes that the powers of the Board of Directors may be limited by express provisions in the articles of incorporation or by an agreement among all shareholders under section 7.32.MBCA.<sup>16</sup> Obviously, some form of governance is necessary for every corporation. The Board of Directors is the traditional form of governance but it need not be the exclusive form. Patterns of management may be tailored to specific needs in connection with family-controlled enterprises, wholly or partially owned subsidiaries, or corporate joint ventures through a shareholder agreement. But, if the corporation does not have a shareholders’ agreement, or if it is a public corporation, it must adopt the traditional Board of Directors as its governing body.<sup>17</sup>
- The phrase ‘by or under the direction, and subject to the oversight, of’, means the varying positions of Boards of directors of different corporations. In some closely held

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certificate of incorporation. If any such provision is made in the certificate of incorporation , the powers and duties of the Board of Directors must be exercised or performed to such an extent

<sup>16</sup> American Bar Association. Committee on Corporate Laws, Model business corporation act annotated : official text with official comments and statutory cross-reference, revised through 2005; adopted by the Committee on Corporate Laws of the Section of Business Law, with the support of the American Bar Association, Section of Business Law (hereinafter MBCA, Official Comment, 2005)

<sup>17</sup> *MBCA, Official Comment, 2005*

corporations, the Board of directors may be involved in the day-to-day business and affairs and it may be reasonable to describe management as being ‘by’ the Board of directors. But in many other corporations, the business and affairs are managed ‘under the direction, and subject to the oversight, of’ the Board of directors, since operational management is delegated to executive officers and other professional managers.<sup>18</sup>

- While providing for corporate powers to be exercised under the authority of the Board of Directors, allows the board of directors to delegate to appropriate officers, employees or agents of the corporation the authority to exercise powers and perform functions not required by law to be exercised or performed by the Board of Directors itself, responsibility to oversee the exercise of that delegated authority nonetheless remains with the board of directors. The scope of that oversight responsibility will vary depending on the nature of the corporation’s business.<sup>19</sup>

## **Boards and Board Committees**

### ***Number of Board members***

Most states in the US permit a Board of Directors to consist of one or two directors. There are some states that limit the right to having one or two directors to corporations with one or two shareholders. The MBCA 1986, and the statutes of an increasing number of states, says that any corporation may elect to have aboard consisting of one or two directors regardless of the number of shareholders.<sup>20</sup> The number of directors of a corporation may be specified

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<sup>18</sup> MBCA, *Official Comment*, 2005

<sup>19</sup> MBCA, *Official Comment*, 2005

<sup>20</sup> MBCA, 1984, par. 2.05: (1) *If initial directors are named in the Articles of Incorporation, the initial directors shall hold an organizational meeting, at the call of a majority of the directors, to complete the organization of*

in or fixed in accordance with the Articles of Incorporation or by-laws. The number of directors can be fixed by the board itself, if authorized by the Articles or by-laws, or if the board is given the power to amend the by-laws. The power of the Board of Directors to fix its size by shareholders' approval is restricted, unless it is not more than 30%. These provisions give the Boards limited power to add a certain number of members without shareholders' approval or to decide not to fill vacancies, but do not give unlimited power to make substantial changes.

### ***Qualifications***

There are no mandatory qualifications requirements for corporate board members in US. According to the MBCA, 1984, a director need not be a resident of the state or shareholder of the corporation unless the Articles of Incorporation or by-laws so prescribe. This means that directors authorized to amend the by-laws can impose residency or status of a shareholder as a qualification to be a Director.

### ***Electing Directors on Board by shareholders - Cumulating voting system***

Cumulative voting means that each shareholder has the number of votes equal to the number of shares owned. It is a system of voting for corporate directors in which each shareholder is entitled to as many votes as they have, times the number of directors to be elected. The shareholder may cast all his votes for a single director or apportion the votes among the candidates. As described above, under the MBCA, shareholders are not permitted to cumulate their votes unless the Articles of Incorporation provide otherwise. If Directors are

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*the corporation by appointing officers, adopting by-laws, and carrying on any other business brought before the meeting; (2) If initial directors are not named in the Articles, the incorporator or incorporators shall hold an organizational meeting at the call of a majority of the incorporators: to elect directors and complete the organization of the corporation; or to elect a Board of Directors who shall complete the organization of the corporation.*

elected by different voting groups, the articles of incorporation may provide that specified voting groups are entitled to vote cumulatively while others are not.

### ***Board Tenure***

In a classified Board, directors are divided into separate classes so that only one class of directors is elected each year. Normally, Boards are divided into three classes, so only one-third of directors are elected each year. According to the MBCA, 1984, the Articles of Incorporation may provide for staggering the terms of directors into two or three classes, each class to be nearly as equal in number as possible, provided that the board consists of nine or more directors.

The MBCA authorizes vacancies in the Board of Directors to be filled either by the shareholders or by the Board of Directors. Directors elected to fill the vacancies must stand for election at the next annual meeting of shareholders even if the term would continue beyond that meeting.

### ***Quorum***

The Board of Directors of a corporation consists of one or more members. Any vacancy occurring in the Board of Directors may be filled by the affirmative vote of a majority of the remaining directors though less than a quorum of the board of director.

### ***Other mandatory requirements***

According to the MBCA, the articles of incorporation must set forth in addition to the name and address of each incorporator, a corporate name for the corporation, the number of shares the corporation is authorized to issue, the street address of the corporation's initial registered office, also the name of its initial registered agent at that office. The articles of incorporation



must among other matters set forth the names and addresses of the individuals who are to serve as the initial directors.

### ***Board of Directors***

Section 8.25 (d, e) of the MBCA, prohibits the delegation of authority with-respect to most mergers, sales of substantially all assets, amendments to Articles of Incorporation and voluntary dissolution under Section 8.25 (e) (2) of the MBCA, since these require shareholder action.<sup>21</sup>

*The official comments on the MBCA ‘Section 8.25 makes explicit the common law power of a Board of Directors to act through committees of directors and specifies the powers of the Board of Directors that are not delegable, that is, powers that only the full Board of Directors may exercise.’ According to the official comment on par. 8.25 of the MBCA, the statement on non-delegable functions is based on the principle that prohibitions against delegation should be limited generally to actions*

Par. 8.25 MBCA specifies the powers of the Board of directors that are non delegable, that is, powers that only the board of directors may exercise. This rule deals only with board committees exercising the powers of the board of directors; the board of directors or management however, independently of section 8.25 of this rule, may establish non board committees composed of directors, employees, or others. According to par. 8.25(b), a committee of the board of directors may be created only by the affirmative vote of a majority of the board of directors then in office, or, if greater, by the number of directors

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<sup>21</sup>According to official comment on the MBCA, 1984, par. 8.25., the statutes of several states make non-delegable certain powers not listed in Section 8.25 (e), for exam pie, the power to change the principal corporate office, to appoint or remove officers, to fix director compensation, or to remove agents.

required to take action by the articles of incorporation or the bylaws. This super- majority requirement reflects the importance of the decision to invest board committees with power to act under section 8.25.

Executive committees have long provided guidance to management between meetings of the full board of directors. Audit committees also have a long history of performing essential review and control functions on behalf of the board of directors. In recent years nominating and compensation committees, composed primarily of non-management directors, have also become more widely used by publicly held corporations.

### ***Corporate Governance in UK***

The United Kingdom company law was enacted on 8<sup>th</sup> November 2006.<sup>22</sup> The Companies Act 2006 is an act revised to reform the existing legal framework relating to companies and other forms of business organization, roles and responsibilities of directors', auditors, actuaries (amends also Part 9 of the Enterprise Act 2002), etc.<sup>23</sup> The Companies Act 2006 is a piece of primary legislation that applies to companies directly. A number of provisions were set out in secondary legislation, mainly through regulations and orders.

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<sup>22</sup>Office of Public Sector Information, *Public Acts 2006, Companies Act 2006* (c. 46).

<sup>23</sup> *The government established the Company Law Review Group in 1998 to consider in detail how company law could be modernized. The Company Law Review recommendations became the blueprint for the reforms proposed in the Company Law Reform White Paper issued in March 2005. Following consultation, the White Paper proposals evolved into a draft Bill which was then debated during its passage through Parliament. Finally, the Bill received Royal Assent (official approval) on 8 November 2006*

The Companies Act, 2006 substantially rewrites the 1985 Companies Act replacing almost all of its provisions and also introducing new provisions. The Companies Act, 2006 is modernizing and simplifying company law. It brings among other novelties a clear statutory statement of directors' general duties and clarifies the existing case law based rules.

The Companies Acts, as defined in section 2 of the Companies Act 2006, in so far as they apply to the company; it includes:

- the company law provisions of Companies Act 2006,
- Part 2 of the Companies (Audit, Investigations and Community Enterprise) Act 2004 (c. 27) (community interest companies), and
- the provisions of the Companies Act 1985 (c. 6) and the Companies Consolidation (Consequential Provisions) Act 1985 (c. 9) that remain enforced.

In the UK various other Act pertaining to the companies functioning were also amended. The Financial Services and Markets Act 2000 was one among those which was amended by Companies Act 2006. Substantial amendments were also made earlier when the Companies Act 2004 was enacted. The company law provisions of the 2006 Act (Parts 1 to 39) restate almost all of the provisions of the 1985 Act, together with the company law provisions of the Companies Act 1989 (the 1989 Act) and the Companies (Audit, Investigations and Community Enterprise)<sup>24</sup> Act 2004 (C(AICE) Act 2004).

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<sup>24</sup> *Explanatory Notes, referring to the Companies Act 2006 (c. 46) which received Royal Assent on 8 November 2006.*

The UK Company law repeals by Companies Act 2006 has refereed various sources before enacting the Companies Act 2006. There includes:<sup>25</sup>

- Companies Act 1985 (c. 6) and Companies Act 1989 (c. 40)
- Insolvency Act 1985 (c. 65)
- Building Societies Act 1986 (c. 53)
- Finance Act 1988 (c. 39)
- Charities Act 1992 (c. 41)
- Trade Marks Act 1994 (c. 26)
- Financial Services and Markets Act 2000 (c. 8)
- Limited Liability Partnerships Act 2000 (c. 12)
- Enterprise Act 2002 (c. 40) in Schedule 17, paragraphs 3 to 8.
- Companies (Audit, Investigations and Community Enterprise) Act 2004 (c. 27)
- Civil Partnership Act 2004 (c. 33)
- Constitutional Reform Act 2005
- Companies (Audit, Investigations and Community Enterprise) Act 2004 (c. 27)
- Limited Partnerships Act 1907 (c. 24)
- Business Names Act 1985 (c. 7)
- Civil Partnership Act 2004 (c. 33)
- The UK Corporate Governance Code (September 2014)

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<sup>25</sup> *Ibidem.*

According to Section 19 of the 2006 Companies Act, a company must have articles of association prescribing regulations for the company.

The Secretary of State may by regulations prescribe Model articles of association for companies and a company may adopt all or any of the provisions of model articles. Section 20 of the 2006 Companies Act defines so called default application of Model articles. Model articles are applied in the formation of a limited company if articles are not registered, or if articles are registered, in so far as they do not exclude or modify the relevant model articles. In other words, if limited companies do not register their own articles of association, Model articles apply by default.<sup>26</sup>

The relevant model articles form part of the company's articles in the same manner and to the same extent as if articles, in the form of those articles had been duly registered.<sup>27</sup> The 2006 Act articles applies to companies formed under the 2006 Act on or after 1st October 2009.<sup>28</sup>

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<sup>26</sup> *Companies Act 2006, Explanatory Notes (These Notes refer to the Companies Act 2006 (c. 46) which received Royal Assent on 8 November 2006: Section 19 of the 2006 Act enables the Secretary of State to prescribe model forms of articles for different descriptions of companies. Under section 20 these model articles will operate as default articles for limited companies formed under the 2006 Act. This replaces section 8 of the 1985 Act and goes wider than that section in extending to private companies limited by guarantee that currently have to register articles and cannot rely on model articles.)*

<sup>27</sup> *This replaces section 8 of the 1985 Act extending to private companies limited by guarantee.*

<sup>28</sup> *Explanatory memorandum to the companies (model articles) regulations 2008, 2008 no. 3229: The version of the model articles that is in force at the time that a particular company is originally registered continues to apply to that company. The 2006 Act model articles will apply to companies formed under the 2006 Act on or after 1 October 2009.*

### **UK Corporate Governance Code (September 2014)**

The Main Principles of the Code of is a guide to a number of key components of effective board practice. It is based on the underlying principles of all good governance: accountability, transparency, responsibilities of directors, probity and focus on the sustainable success of organizations for longer term.

The Financial Reporting Council (FRC) is responsible for promoting high quality corporate governance and reporting to foster investment. The UK Corporate Governance, Stewardship Codes and UK standards for accounting, auditing and actuarial work are been supported by the FRC. The FRC is also responsible for setting the international standards for the corporate in UK. FRC also monitor and take action to promote the quality of corporate reporting and auditing. FRC operates independently to promote the corporate governance standards, regulatory issues, auditing mechanisms among the UK corporate.

The codes focused on the various provisions for companies about the information on the risks which affect the long-term viability. This information needs to be shared with the investors. The companies needs to present information to give a clearer and broader view of their performance, solvency, liquidity, risk management and viability. I addition, boards of listed companies would also need to ensure that executive remuneration is aligned to the long-term success of the company and demonstrate more clearly to its shareholders.

**Figure 4.2 : FRC Code on CG**



### **Leadership issues**

There should be a clear division of responsibilities at the head of the company between the running of the board and the executive responsibility for the running of the company's business. Individual should have unfettered powers of decision. The chairman is responsible for leadership of the board and ensuring its effectiveness on all aspects of its role.

### **Effectiveness issues**

The board and its committees should have the appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively. There should be a formal, rigorous and transparent procedure for the appointment of new directors to the board. All directors should be able to allocate sufficient time to the company to discharge their responsibilities effectively.

All directors should receive induction on joining the board and should regularly update and refresh their skills and knowledge. The board should be supplied with timely information in

a manner with information in a form and of a quality appropriate to enable it to discharge its duties. The board undertakes a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors. All directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance.

### **Accountability issues**

The board presents a fair, balanced and understandable assessment of the company's position and prospects. The board is responsible for determining the nature and extent of the principal risks that could support the strategic objectives. The board should maintain sound risk management and internal control systems. The board should establish formal and transparent arrangements for considering how they should apply the corporate reporting, risk management and internal control principles and for maintaining an appropriate relationship with the company's auditors.

### **Remuneration issues**

Executive directors' remuneration is designed to promote the long-term success of the company. Performance-related pays and perks should be transparent, stretching and rigorous. There should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors. No director should be involved in deciding his or her own remuneration.

### **Relations with shareholders issues**



There should be a dialogue with shareholders based on the mutual understanding of the organizational objectives. The board as a whole has responsibility for ensuring that a satisfactory dialogue with shareholders. The board conducts general meetings to communicate information to its investors and support them to actively participate in the meetings to enable the company to benefit from their interactions.

### **Composition of the Board of Directors**

There is only a single Board of Directors in the UK and, according to the UK Companies Act of 2006 (section 154) companies are required to have directors, who are natural persons:

- a private company must have at least one director;
- a public company must have at least two directors.

Pursuant to Companies Act 2006, a private company needs only to have one Director, unless the Articles of Association of the Company require a greater number to be appointed. A public company must always have at least two Directors, although the Articles may require a greater number.

### **Appointments of Directors**

The UK Companies Act 2006 provides ways of appointing the Directors, as mentioned in the AoA of the company. The Act does not require that all Directors be elected by the shareholders in general meeting. In addition, the Act does not require that Directors must submit themselves periodically to re-election by the shareholders.

However, the Act provides that all the appointment must be voted individually (except in the case of a private company, unless the shareholders' meeting agrees otherwise). The Section 160/1 prescribes the way of decision taking on appointing directors: 'At a general meeting of a public company a motion for the appointment of two or more persons as directors of the company by a single resolution must not be made unless a resolution that it should be so made has first been agreed to by the meeting without any vote being given against it.' It is common that a member holding 51% of the voting shares elects all members of the board. The Companies Act 2006 does not provide for cumulative voting, which gives the shareholder the right to be represented on the board in proportion with his holding.

### **Removal of Directors**

Section 168 of the Companies Act 2006 (Resolution to remove a Director) provides that an ordinary resolution is sufficient to remove a Director, before the expiration of his period of office, notwithstanding anything in any agreement between it and him. Special notice is required to remove a Director or to appoint. In case the decision is taken during the board meeting also, a special notice to be circulated.<sup>6</sup> On receipt of notice of an intended resolution to remove a director under Section 168, the company must forthwith send a copy of the notice to the Director concerned. The Director (whether or not a member of the company) is entitled to be heard on the resolution at the meeting. On the resolution at the meeting, the Director (whether or not a member of the company) is entitled to be heard on the resolution at the meeting.

### ***Qualification, Vacation of Office***

The minimum age for appointment as director is introduced by Companies Act 2006: ‘A person may not be appointed as director of a company unless he has attained the age of 16 years.’

*Section 168/4: ‘A person appointed Director in place of a person removed under this section is treated, for the purpose of determining the time at which he or any other Director is to retire, as if he had become Director on the day on which the person in whose place he is appointed was last appointed a Director.’*

Articles usually provide for the vacation of office by Directors in certain circumstances, as for instance in case of resignation, prolonged absence from board meetings, insanity or age (e.g. age of 70). Besides natural persons even a legal entity can be appointed as Director, unless they are prohibited by-law from holding office. It is often in practice that a parent company acts as a Director to perform the complete control of a subsidiary.

### **Committees**

The Articles may authorize the Directors to delegate any of their powers to committees of Directors and to appoint one or more of their body to act as managing Directors (Articles 72 and 74). The Directors may delegate any of their powers to different kinds of committees (executive committee, auditing committee, and nominating committee, compensating committee). Committees must follow procedures which are based on provisions of the

articles governing the decision making by directors. The Directors may make rules of procedure for all or any committees. The rules of procedure made by Directors may prevail over rules derived from the articles if they are not consistent with them.<sup>29</sup> The Articles usually provide rules governing the proceedings of the committees.

### **Corporate Governance in Australia**

The governance attributes of organisation in Australia include both "internal" (e.g. constitution, organisational policies) and "external" (e.g. laws, regulations, community expectations) factors. A board of directors plays a pivotal role in influencing an organization's governance environment. The common goals of organisations are to follow effective governance framework in place that best fits the individual and organizations as a whole. The key challenge of corporate governance is to drive the organisational performance while aiding conformance with requirements of the stakeholders. An effective governance framework should contribute to the individual directors; to enhance the effectiveness of the board and board performance; way in which governance is applied throughout the organisation; strengthen relationships with its stakeholders. Governance practices a listed entity chooses to adopt is fundamentally a matter for its board of directors, the body charged with the legal responsibility for managing its business with due care and diligence and therefore for ensuring that it has appropriate governance arrangements in place. The ASX Corporate Governance Council's Recommendations, 2010 were not mandatory as these principles do not prevent corporate failure or poor corporate

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<sup>29</sup> *Model Articles*

decision-making. There are eight core principles (the Principles). They are intended to provide a reference point for companies about their corporate governance structures and practices. These Principles are discussed below:

Principle 1 – Lay solid foundations for management and oversight Companies should establish and disclose the respective roles and responsibilities of board and management.

Companies should establish the functions reserved to the board and those delegated to senior executives and disclose those functions. Companies should provide the information indicated in the Guide.

Principle 2 - Structure the board to add value Companies should have a board of an effective composition, size and commitment to adequately discharge its responsibilities and duties. A majority of the board should be independent directors. The chair should be an independent director. The roles of chair and chief executive officer should not be exercised by the same individual.

Principle 3 - Promote ethical and responsible decision-making Companies should actively promote ethical and responsible decision-making. The practice takes into account their legal obligations and the reasonable expectations of their stakeholders the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.

Principle 4 - Safeguard integrity in financial reporting Companies should have a structure to independently verify and safeguard the integrity of their financial reporting. The board should establish an audit committee. The audit committee should be structured so that it: consists only of non-executive directors consists of a majority of independent directors is chaired by an independent chair, who is not chair of the board has at least three members.

Principle 5 - Make timely and balanced disclosure Companies should promote timely and balanced disclosure of all material matters concerning the company. Companies should establish written policies designed to ensure compliance with ASX Listing Rule disclosure requirements and to ensure accountability at a senior executive level for that compliance and disclose those policies or a summary of those policies.

Principle 6 - Respect the rights of shareholders Companies should respect the rights of shareholders and facilitate the effective exercise of those rights. Companies should design a communications policy for promoting effective communication with shareholders and encouraging their participation at general meetings and disclose their policy or a summary of that policy.

Principle 7- Recognize and manage risk Companies should establish a sound system of risk oversight and management and internal control. The board should require management to design and implement the risk management and internal control system to manage the company's material business risks and report to it on whether those risks are being managed effectively. The board should disclose that management has reported to it as to the effectiveness of the company's management of its material business risks. The board should disclose whether it has received assurance from the chief executive officer (or equivalent) and the chief financial officer (or equivalent) that the declaration provided in accordance with section 295A of the Corporations Act is founded on a sound system of risk management and internal control and that the system is operating effectively in all material respects in relation to financial reporting risks.

Principle 8- Remunerate fairly and responsibly Companies should ensure that the level and composition of remuneration is sufficient and reasonable and that its relationship to performance is clear.

### **Boards and Board Committees**

A high performing, effective board is essential for the proper governance of a listed entity. The board needs to have an appropriate number of independent non-executive directors who can challenge management and hold them to account, and also represent the best interests of the listed entity and its security holders as a whole rather than those of individual security holders or interest groups. The board should be of sufficient size so that the requirements of the business can be met and changes to the composition of the board and its committees can be managed without undue disruption. However, it should not be so large as to be unwieldy. The general directors' duties, you also have a positive duty to prevent your company trading if it is insolvent. A company is insolvent if it is unable to pay all its debts when they are due. This means that before you incur a new debt, you must consider whether you have reasonable grounds to suspect that the company is insolvent or will become insolvent as a result of incurring the debt.

An understanding of the financial position of your company only at the time you sign off on the yearly financial statements is insufficient. To be aware constantly company's the board should monitor the financial position. Regulatory Guide 217 highlights the duties to prevent insolvent trading and guide the directors to maintain the financial records and explain

transactions. A failure of a director to take all reasonable steps to ensure a company fulfils this requirement contravenes the Corporations Act.

### ***Board Size***

The size of a board is a factor that can influence its effectiveness. The main point here is that bigger is not necessarily better. The constitutions of NFPs often specify a maximum or actual board size. Some constitutions provide for relatively large boards (e.g. ten or twelve directors), commonly with the intention that the board is “representative” of its membership (e.g. geographical representation for federated structures), the community the NFP serves, etc.

### ***Audit Committee***

While ultimate responsibility for a listed entity’s financial statements rests with the full board, having a separate audit committee can be an efficient and effective mechanism to bring the transparency, focus and independent judgement needed to oversee the corporate reporting process.

### ***Nomination Committee***

Having a separate nomination committee can be an efficient and effective mechanism to bring the transparency, focus and independent judgement needed on decisions regarding the composition of the board.

### ***Risk Committee***

The risk committee (be it a stand-alone risk committee, a combined audit and risk committee or a combination of board committees addressing different elements of risk) is an efficient and effective mechanism to bring the transparency, focus and independent



judgement needed to oversee the entity's risk management framework. A risk committee should be of sufficient size and independence, and its members between them should have the necessary technical knowledge and a sufficient understanding of the industry in which the entity operates, to be able to discharge the committee's mandate effectively.

### ***Remuneration Committee***

The remuneration committee should be of sufficient size and independence to discharge its mandate effectively. Having a separate remuneration committee can be an efficient and effective mechanism to bring the transparency, focus and independent judgement needed on remuneration decisions.

### ***Board Assessment***

A listed entity should have and disclose a board skills matrix setting out the mix of skills and diversity that the board currently has or is looking to achieve in its membership. Boards "skills matrix" is a useful tool that can help identify any gaps in the collective skills of the board that should be addressed as part of a listed entity's professional development initiatives for directors and in its board succession planning. Disclosing the mix of skills and diversity that a board currently has or is looking to achieve in its membership is useful information for investors and increases the accountability of the board on such matters. The disclosure need only be made collectively across the board as a whole, without identifying the presence or absence of particular skills by a particular director.

## **Corporate Governance in Singapore**

Corporate Governance is a 'Culture' which tones the top management emphasizing them to follow the guidelines to cultivate effective corporate governance among the listed companies in Singapore. Due to the changing global scenarios, the corporate governance structure in Singapore has undergone tremendous changes since 2007. This was due to the corporate failures in Singapore followed by global financial crises. During 2009, Singapore Exchange (SGX) prepared and circulated a consultation paper and the suggestions were implemented during 2011. This helped the state to have a greater control over the listed enterprise in Singapore Exchange. The key suggestion was to implement the internal control system in the listed enterprises. The Singapore Companies Act 1999 was reviewed by the Company Legislation and Regulatory Framework Committee. The New Companies Act highlighted on the ensuring an effective, efficient and transparent corporate regulatory framework aimed to attract the international investors into the country. The Monetary Authority Singapore issued guidelines of CG for Banks and financial institutions during 2010.

### **Boards and Board Committees**

Companies should be headed by effective Board members to lead and control the operations. The Boards and Board committees are collectively responsible for the long-term success of the company. The Boards work with stakeholders to achieve corporate objectives.

The following are the duties of the boards :

All directors must objectively discharge their duties and responsibilities at all times as fiduciaries in the interests of the company. The Board may delegate the authority to make decisions to any board committee but without abdicating its responsibility. Any such delegation should be disclosed in either the Corporate Governance policy or Blueprint of CG framework. The following are the fiduciary duties of the boards :

- There should be a strong and independent element on the Board, which is able to exercise objective judgement on corporate affairs independently, in particular, from Management and 10% shareholders
- No individual or small group of individuals should be allowed to dominate the Board's decision making.
- There should be a strong and independent element on the Board, with independent directors making up at least one-third of the Board.

### **Independent Directors**

The independent directors should make up at least half of the Board. An "independent" director is one who has no relationship with the company. The major role of the ID is to

*“Exercise independent business judgment with a view to the best interests of the company”.*

The Board should identify in the company's Annual Report each director it considers to be independent. The Board should determine, taking into account the views of the Nominating Committee (NC), whether the director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director's judgement. Directors should disclose to the Board any such

relationship as and when it arises. The Board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination, including the following:

- a director being employed by the company or any of its related corporations for the current or any of the past three financial years;
- a director who has an immediate family member who is, or has been in any of the past three financial years, employed by the company or any of its related corporations and whose remuneration is determined by the remuneration committee;
- a director, or an immediate family member, accepting any significant compensation from the company or any of its related corporations for the provision of services, for the current or immediate past financial year, other than compensation for board service;
- a director:
  - i. who, in the current or immediate past financial year, is or was; or
  - ii. whose immediate family member, in the current or immediate past financial year, is or was,
    - a 10% shareholder of, or a partner in (with 10% or more stake), or an executive officer of, or a director of, any organisation to which the company or any of its subsidiaries made, or from which the company or any of its subsidiaries received, significant payments or material services (which may include auditing, banking, consulting and legal services), in the current or

immediate past financial year. As a guide, payments<sup>5</sup> aggregated over any financial year in excess of \$200,000 should generally be deemed significant;

- a director who is a 10% shareholder or an immediate family member of a 10% shareholder of the company; or
- a director who is or has been directly associated with a 10% shareholder of the company, in the current or immediate past financial year.

The relationships set out above are not intended to be exhaustive, and are examples of situations which would deem a director to be not independent. The Board inspite of the existence of one or more of these relationships, to consider the director as independent, it should disclose in full the nature of the director's relationship and bear responsibility for explaining why he should be considered independent.

The independence of any director who has served on the Board beyond nine years from the date of his first appointment should be subject to particularly rigorous review. In doing so, the Board should also take into account the need for progressive refreshing of the Board. The Board should also explain why any such director should be considered independent.

The Board should examine its size and, with a view to determining the impact of the number upon effectiveness, decide on what it considers an appropriate size for the Board, which facilitates effective decision making. The Board should take into account the scope and nature of the operations of the company, the requirements of the business and the need to avoid undue disruptions from changes to the composition of the Board and board committees. The Board should not be so large as to be unwieldy.

The Board and its board committees should comprise directors who as a group provide an appropriate balance and diversity of skills, experience, gender and knowledge of the company. They should also provide core competencies such as accounting or finance, business or management experience, industry knowledge, strategic planning experience and customer-based experience or knowledge.

Non-executive directors should:

- constructively challenge and help develop proposals on strategy; and
- review the performance of Management in meeting agreed goals and objectives and monitor the reporting of performance.

To facilitate a more effective check on Management, non-executive directors are encouraged to meet regularly without the presence of Management.

### ***Audit Committee***

The Board should establish an Audit Committee ("AC") with written terms of reference which clearly set out its authorities and duties. The AC should comprise at least three directors, the majority of whom, including the AC Chairman, should be independent. All of the members of the AC should be non-executive directors. The Board should disclose in the company's Annual Report the names of the members of the AC and the key terms of reference of the AC, explaining its role and the authority delegated to it by the Board. The Board should ensure that the members of the AC are appropriately qualified to discharge their responsibilities. At least two members, including the AC Chairman, should have recent and relevant accounting or related financial management expertise or experience, as the Board interprets such qualification in its business judgement. The AC should have explicit

authority to investigate any matter within its terms of reference, full access to and co-operation by Management and full discretion to invite any director or executive officer to attend its meetings, and reasonable resources to enable it to discharge its functions properly

### **Corporate Governance in Malaysia**

Ever since the 1980s, the governance of the Malaysian has experienced a lot of transformations as a result of various improvements and modernization. In addition, the Malaysian government aims to be ranked into the top 30 of the Transparency International's Corruption Perception Index (CPI) by year 2020. However, CPI of Malaysia since year 2008 to 2011 somehow showing that the public comprehend business ethics in Malaysia is still not as to be expected. Furthermore, there are a number of corporate governance issues arise in Malaysian.

Malaysia is struggling to become a developed nation in its own frame by 2020. With the aim to become a successful developing country, Malaysian Government is working hard to strengthen corporate governance framework to ensure citizens quality of life are continuously improve. The biggest challenge within corporate governance framework is to strengthen the ethics and integrity framework. Lack of integrity value within individuals and organisations as well as society at large can lead to many negative consequences such as corruption, irregularities, misuse of power, deception, unethical practices as well as increasing crime rate. Malaysian recently listed at number 39 out of 159 countries with a score of 5.1 in the CPI. The introduction of the National Integrity Plan (NIP) is to reduce the

level of Transparency International (TI) to 30. The Bribe Payers Index Ranking in year the 2002 presented Malaysia at number 15 out of 21.

Currently, there are a number of issues arising out of the policy of the Malaysian government that negatively affect the governance of the GLC's in the country. As such, compliance to blueprint of CG is important to achieve the trust of the community and ensure a good flow of capital by attracting foreign investors to benefit the economic of the nation. Corporate Governance refers to the process and structure used to direct and manage the business and affairs of the company towards enhancing business prosperity and corporate accountability with the ultimate objective of realizing long term shareholder value, whilst taking account the interests of other stakeholders. On the other hand, from the economic perspective, corporate governance is an important element of achieving an allocative efficiency in which scarce funds are moved to investment project with the highest returns. In practice, efficiency is achieved when at given level of risk, investments project offer the highest return exceeding its cost of capital. The crisis indicated how the failure to regulate good governance affected the mobilization of funds in an effective way. As such strong good governance policy is crucial for Malaysian companies to increase corporate accountability and to avoid massive disasters before they occur.

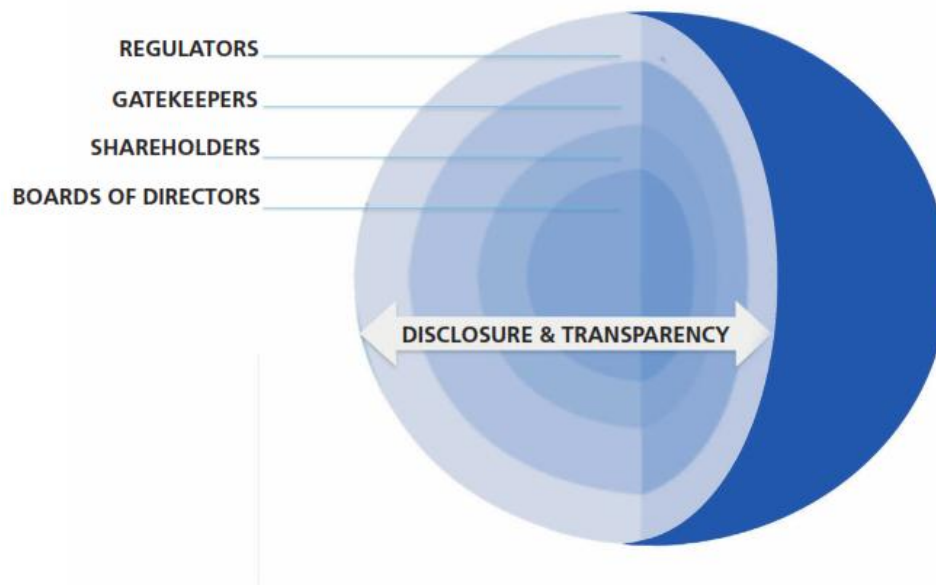
### **Corporate Governance Policy**

The principles of Malaysian Corporate Governance(CG) policy and recommendations focus on, a strong foundation for the board and its committees to carry out their roles



effectively, promote timely and balanced disclosure, safeguard the integrity of financial reporting, emphasize the importance of risk management and internal controls and encourage shareholder participation in general meetings. The aims of this CG policy is to provide guideline to business entity so that the entire business activities embrace best corporate governance practice especially among Government linked Companies because more than half of the paid up capital mainly contributed by the government through taxpayers' money. As such the public expectation towards GLCs is very high. In Malaysia, GLCs were established to enhance the functions of government services to the public in terms of administration, transportation, communication and so on. Unfortunately, past studies have shown that GLCs lack of good governance practices compared to non-GLCs.

**Figure 4.3 : Corporate Governance Ecosystem**



Several GLCs are suffers from poor performances such as Malaysian Airline System (MAS) and Proton Holding Berhad. Hence due to poor governance and management. GLCs need to ensure good governance so that they will be able to meet the requirements and expectations of the government through outstanding business performance (Lawler & Mohrman, 2013). Khazanah (2014) stated that with strong governance GLCs are anticipated to be able to improve performance. As such seven (7) CG principles was outlined as a guideline to corporate sector including GLCs to ensure business conduct are free from negative elements such as wastage, mismanagement and corruption. A company can reduce the amount of risks in their business as well as any attempts of corruption and mismanagement by following the practices of good governance. Due to the amount of transparency necessary in companies that follow the principles of good governance, many individuals intending to misuse their position and power will be unable to do so. This will reduce the overall

incidences of negative acts in the company and help it achieve success and a positive image in the community.

*Principle 1:* Establish clear roles and responsibilities : The responsibilities of the board, which should be set out in a board charter, include management oversight, setting strategic direction premised on sustainability and promoting ethical conduct in business dealings.

Recommendation:

- The board should establish clear functions reserved for the board and those delegated to management.
- The board should establish clear roles and responsibilities in discharging its fiduciary and leadership functions.
- The board should formalise ethical standards through a code of conduct and ensure its compliance.
- The board should ensure that the company's strategies promote sustainability.
- The board should have procedures to allow its members access to information and advice.
- The board should ensure it is supported by a suitably qualified and competent company secretary.
- The board should formalise, periodically review and make public its board charter.

*Principle 2:* Strengthen Composition: The board should have transparent policies and procedures that will assist in the selection of board members. The board should comprise members who bring value to board deliberations.

Recommendation:

- The board should establish a Nominating Committee which should comprise exclusively of nonexecutive directors, a majority of whom must be independent.
- The Nominating Committee should develop, maintain and review the criteria to be used in the recruitment process and annual assessment of directors.
- The board should establish formal and transparent remuneration policies and procedures to attract and retain directors.

Principle 3: Reinforce Independence. The board should have policies and procedures to ensure effectiveness of independent directors.

Recommendation:

- The board should undertake an assessment of its independent directors annually.
- The tenure of an independent director should not exceed a cumulative term of nine years. Upon completion of the nine years, an independent director may continue to serve on the board subject to the director's re-designation as a non-independent director.
- The board must justify and seek shareholders' approval in the event it retains as an independent director, a person who has served in that capacity for more than nine years.
- The positions of chairman and CEO should be held by different individuals, and the chairman must be a non-executive member of the board.

- The board must comprise a majority of independent directors where the chairman of the board is not an independent director

*Principle 4: Foster Commitment:* Directors should devote sufficient time to carry out their responsibilities, regularly update their knowledge and enhance their skills.

Recommendation:

- The board should set out expectations on time commitment for its members and protocols for accepting new directorships.
- The board should ensure its members have access to appropriate continuing education programmes.

*Principle 5: Uphold integrity in financial reporting:* The board should ensure financial statements are a reliable source of information.

Recommendation:

- The Audit Committee should ensure financial statements comply with applicable financial reporting standards.
- The Audit Committee should have policies and procedures to assess the suitability and independence of external auditors.

*Principle 6: Recognise and manage risks:* The board should establish a sound risk management framework and internal controls system.

Recommendations

- The board should establish a sound framework to manage risks.
- The board should establish an internal audit function which reports directly to the Audit Committee.

*Principle 7:* Ensure timely and high quality disclosure : Companies should establish corporate disclosure policies and procedures to ensure comprehensive, accurate and timely disclosures.

**Table 4.2 : CG Milestones in Malaysia**

<b>Year</b>	<b>Milestone</b>
1999	<ul style="list-style-type: none"> <li>• High level finance committee report on Corporate Governance</li> </ul>
2000	<ul style="list-style-type: none"> <li>• Malaysian Code on Corporate Governance (CG Code)</li> <li>• Minority Shareholder Watchdog Group (MSWG)</li> </ul>
2001	<ul style="list-style-type: none"> <li>• Capital Market Masterplan (CMP)</li> <li>• First Corporate Governance Report on the Observance of Standards and Codes (CG ROSC)</li> <li>• Corporate Governance requirements incorporated into the Kuala Lumpur Stock Exchange</li> </ul>
2004	<ul style="list-style-type: none"> <li>• Whistleblowing provisions in securities laws</li> </ul>
2005	<ul style="list-style-type: none"> <li>• Second CG ROSC commenced</li> </ul>
2007	<ul style="list-style-type: none"> <li>• Qualification criteria for directors introduced, audit committee strengthened and internal audit function mandated</li> <li>• Enforcement powers for civil and administrative actions expanded to allow recovery of up to three times the amount of losses for a wider range of market misconduct offences</li> <li>• MSWG guide of the Best Practices for Institutional Shareholders</li> </ul>

2009	<ul style="list-style-type: none"> <li>• The SCs enforcement powers broadened by the introduction of sections 317A and 320A of the Capital Markets and Services Act 2007 (MCA)</li> </ul>
2010	<ul style="list-style-type: none"> <li>• Audit Oversight Board (AOB)</li> </ul>
2011	<ul style="list-style-type: none"> <li>• Securities Industry Dispute Resolution Centre (SIDREC)</li> <li>• Capital Market Masterplan 2 (CMP2)</li> </ul>

Source : Malaysian Code on Corporate Governance, 2012, Securities Commission Malaysia

### **Blueprint of Corporate Governance Framework in Malaysia**

In 2011, Corporate Governance Blueprint was issued by SC. This Corporate Governance Blueprint represents another significant milestone in our journey which recognises that, from time to time, a major review and recalibration of controls is necessary to ensure that Malaysia's corporate governance framework remains relevant and effective. This Blueprint is an affirmation of our commitment to achieve nothing less than excellence in governance.

### **Securities Commission (SC)**

The establishment of the Securities Commission (SC) in March 1993 was set up to improve the legal and regulatory framework governing the capital market. The Securities Industries Act (SIA) 1983 and Securities Commission Act (SCA) 1993, under the authority of the Ministry of Finance, represent the legislative and regulatory framework of Malaysia's capital market. With the establishment of the SIA, the Companies Commission of Malaysia (CCM) (formerly known as the Registrar of Companies-ROC) was established to introduce the Code of Ethics for Directors in 1996 as an initiative to create effective boards. A survey by the Asian Development Bank found that Malaysia had the highest level of effective boards

of directors as a supervision body compared to other East Asian countries - Korea, Indonesia, Philippines and Thailand.

### **The Malaysian Capital Market Master Plan (CMP)**

An important initiative of the Securities Commission was the Malaysian Capital Market Master Plan (CMP). The CMP 1 was launched in February 2001 and it reflected the government's proactive response to ensure the recommendations contained in the Report on Corporate Governance will be affected in a timely and comprehensive manner. In the CMP, 10 out of 152 recommendations deal with the development of the institutional and regulatory framework for the capital market from 2001 to 2010. These focus specifically on the corporate governance issues. Further, the establishment of the Corporate Law Reform Committee, in August 2003, is to spearhead the corporate law reform programme. It is seen as another milestone for the success of corporate governance reforms in Malaysia where corporate governance issues are high on the priority of the committee. Malaysia continues to move forward with plans to transform into a developed economy by 2020.

The Capital Market Masterplan 2 (CMP2) was launched in April 2011 to expand the role of the capital market in invigorating national economic growth. It is a major philosophy of CMP2 that growth is only sustainable if it is underpinned by a proper system of accountabilities and governance. Strengthening corporate governance therefore represents one of the key thrusts to reinforce investor trust and confidence in the Malaysian capital market. In CMP 2, boards of companies occupy a central role as agents of shareholders,



both retail and institutional, within the corporate governance ecosystem. Boards in turn are directly influenced by shareholders who through exercising their rights as owners can ensure responsible actions by companies. Gatekeepers and influencers, interposed between the company and shareholders, have an important role in promoting self and market discipline, thereby reducing the need for regulatory discipline. Lastly public and private enforcement plays a crucial role in ensuring that corporate governance transgressors are held accountable through actions by the state, regulators or aggrieved parties.

### **Companies Commission of Malaysia and the Corporate Law Reform Committee (CLRC)**

Another effort for developing an effective and sound corporate governance framework within the corporate law reform programme is the establishment of the CLRC. This initiative was undertaken by the Companies Commission of Malaysia (CCM). The committee was formed to revise, introduce, amend or abolish a good deal of corporate law in an effort to facilitate the development of a business environment which is conducive for Malaysia. This is because, in the past, the amendment to the Companies Act i.e, the SIA and other corporate law legislation was done on a piecemeal basis. In a nutshell, the CLRC is to do with modernising Malaysian company law to be in tandem with the development of company law of other leading common law jurisdictions such as the UK, Singapore and Australia. The government on its part supports the review exercise that is being conducted by the CLRC, as it is committed towards ensuring that the corporate regulatory framework in Malaysia continues to promote enterprise and competitiveness. Further, this

representation is necessary for a comprehensive, modern and balanced view of the corporate reform in Malaysia.

### **Malaysian Accounting Standard Board (MASB)**

Malaysia became the first country in Asia to set up an independent standard setting body, the Malaysian Accounting Standards Board (MASB), under the Financial Reporting Act (FRA) 1997. The MASB is an independent authority to develop and issue accounting and financial reporting standards in Malaysia, and, under the FRA, all companies listed on the KLSE are required to comply with the accounting standards approved by the MASB. MASB's mission is to develop and promote high quality accounting and reporting standards that are consistent with international best practices for the benefit of users, preparers, auditors and the public in Malaysia with direct contribution towards the international development of financial reporting.

### **The High Level Finance Committee on Corporate Governance and the Malaysian Institute of Corporate Governance (MICG)**

Due to Asian Financial Crisis, the government took proactive action to review and strengthen corporate governance in Malaysia with the establishment of the High Level Finance Committee on Corporate Governance in 1998 comprising 72 government and industry representatives. Its task was to identify and address weaknesses highlighted by the

1997 financial crisis and to establish a framework for corporate governance best practices. Consequently the Malaysian Institute of Corporate Governance (MICG) was established in 1999. The inception of MICG on the other hand is to raise the awareness and good corporate governance practices by businesses and corporate development in Malaysia. The main mission is to improve and promote corporate governance best practices as well as to strengthen corporate governance principles and compliance efforts. Further, it also provides an independent platform for various stakeholders to interact and debate corporate governance issues to promote continuous improvement in corporate governance best practices.

### **The Malaysian Code of Corporate Governance (MCCG) and Bursa Malaysia**

Bursa Malaysia [previously known as Kuala Lumpur Stock Exchange (KLSE)] has adopted most of the recommendations of the Malaysian Code on Corporate Governance 73 (MCCG) 2000 in order to enhance the transparency of public listed companies' disclosure. The Code was brought into full effect in January 2001 with the amendment to the Bursa listing requirement. All listed firms with a financial year ending after 30th June 2001 onwards were required to include in their annual report - the statement of corporate governance, a statement of internal control, composition of the board of directors, composition of audit committee, quorum of audit committee and any additional statements by the board of directors (Kuala Lumpur Stock Exchange, 2001).

The MCCG 2000 established the board of directors as the first principle and under Part 2 (AA) of MCCG 2000, the role, composition and structure of the board of directors are viewed as the most crucial elements for effective corporate governance mechanisms for

Malaysian companies. The Code recommends that firms have a well balanced and effective board to take the lead role in establishing best practice in corporate governance and the code defines a well-balanced board as having a balance of executive directors and non-executive directors, including independent non-executive directors, to ensure effective decision making by the board with no domination from individual or small groups of individuals. Code also requires that nonexecutive directors have the necessary skills and experience and be persons of calibre and credibility in order to bring independent judgment to the board. MCCG 2000 was revised on 2007 and the revised code mainly strived to strengthen the role of audit committee by requiring the committees to comprise fully of non-executive directors. In addition, all its members should be able to read, analyse and interpret financial statements so that they will be able to effectively discharge their functions. The key amendments to the code is aimed at strengthening the Board of directors (BOD) and audit committees and ensuring that BOD and audit committees discharge their roles and responsibilities effectively.

### **The Malaysian Institute of Accountants**

The Malaysian Institute of Accountants (MIA) is a statutory body established under the Accountants Act, 1967 to regulate and develop the accountancy profession in Malaysia. MIA's responsibilities include education and quality assurance as well as enforcement 75 which are carried out to ensure that the credibility of the profession is maintained and that public interest is continuously upheld. In the international and regional arena, MIA plays a significant role in developing and advancing the global accounting profession through its

involvement in organisations such as the International Federation of Accountants and the Confederation of Asian and Pacific Accountants (CAPA).

### **Minority shareholder watchdog group (MSWG)**

Other initiative undertaken was the establishment of the Minority Shareholder Watchdog Group (MSWG) in 2001, which is to encourage independent and proactive shareholder participation in listed companies. MSWG functions as the think-tank and resource centre and as an effective check and balance mechanism on behalf of the minority shareholders to deter abuse from the majority shareholders. The MSWG is a non-profit organisation representing the five largest institutional funds in Malaysia, namely. the Employee Provident Fund (EPF), Lembaga Tabung Angkatan Tentera (LTAT), Lembaga Tabung Haji (LTH), Social Security Organization (SOCSO) and Permodalan Nasional Berhad (PNB).

### **Malaysian Code on Corporate Governance**

The Malaysian Code on Corporate Governance 2012 (MCCG 2012) focuses on strengthening board structure and composition as well as recognizing the role of directors as active and responsible fiduciaries. The MCCG 2012 supersedes the 2007 Code. It sets out eight broad principles and 26 specific recommendations on structures and processes which companies should adopt in making good corporate governance an integral part of their business dealings and culture<sup>30</sup>. According to the Security Commission of Malaysia, some of the key areas that have been strengthened in the MCCG 2012 are as follows:

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<sup>30</sup> Malaysia Code of Governance 2012

- Roles and responsibilities of the board: The board is required to formalize ethical standards through a code of conduct and ensure company strategies promote sustainability. It is also expected to formalize a board charter.
- Composition of the board: The board should establish a Nominating Committee, chaired by a senior independent director, who is responsible to oversee the selection and assessment of directors. The Nominating Committee is charged with developing a set of criteria including policies formalizing its approach to diversity of the board.
- *Independence of independent directors:* The tenure of independent directors is capped to a cumulative period of nine years. Upon completion of the nine years, such directors can be re-designated as non-independent directors or in exceptional circumstances; the shareholders may decide that an independent director can remain in that capacity after serving a cumulative term of nine years. The board should provide strong justification to the shareholders in such exceptional circumstances. The calculation of the tenure starts from the time the individual is first appointed as an independent director of a company. Listed companies should seek shareholders' approval at the nearest AGM before the director reaches the nine year term limit. Shareholders' approval should be sought annually after the nine year term limit. Rotation of independent directors within a group of companies is not advisable. Failure to seek shareholders' approval for the extension of the tenure of any independent director prior to the nine year term limit must be explained in the annual report.

- *Separation of Chairman and CEO:* The positions of Chairman and CEO should be held by different individuals and the chairman must be a non-executive member of the board. Where the Chairman is not an independent director, the board should comprise a majority of independent directors. The term ‘Chairman’ refers to the Chairman of the Board of Directors while the ‘CEO’ refers to the Chief Executive of the company, whatever name called, who may or may not be a member of the board. The responsibilities of the Chairman should include leading the board in the oversight of management, while the CEO focuses on the business day-to-day management of the company and this division should be clearly defined in the board charter. Listed companies that do not comply with any of the recommendations of MCCG 2012, including the separation of positions of chairman and CEO, must explain their circumstances and reasons or justifications for doing so in their annual report.
- *Commitment of directors:* The board is required to set out expectations on time commitment for its members and protocols for accepting new directorships. Directors should notify the chairman before accepting any new directorship. Such notification should include an indication of time commitment expected of the new appointment. The Nominating Committee should take cognisance of such new appointment in its annual assessment of directors.
- *Remuneration of directors:* The board should establish formal and transparent remuneration policies and procedures to attract and retain directors. A Remuneration Committee can perform this function.

- *Risk management framework and internal controls system:* The board is required to establish a sound framework to determine the company's level of risk tolerance and actively identify, assess and monitor key business risks.
- *Integrity of financial reporting:* The Audit Committee should ensure financial statements comply with applicable financial reporting standards and assess the suitability and independence of external auditors. These recommendations are in addition to the requirements of an Audit Committee under the Listing Requirements.
- *Relationship between company and shareholders:* The board should encourage shareholder participation at general meetings and voting on resolutions by way of poll. The chairman should inform shareholders of their rights to demand a poll vote at the commencement of a general meeting. The board is encouraged to put substantive resolutions to vote by poll and make an announcement of the detailed results showing the number of votes cast for and against each resolution. Substantive resolutions are those that are not procedural and administrative in nature; for example, the appointment of directors and auditors, approval for issuance of shares, share buy-backs, related party transactions and resolutions that are tabled by way of supplementary circular to shareholders

The principles of MCCG 2012 encapsulate broad concepts underpinning good corporate governance that companies should apply when implementing the recommendations. The overall objective is for boards to move away from their role as mere advisers to become active and responsible fiduciaries. A culture of good governance in the boardroom therefore



needs to be inculcated as much as the rules themselves and this requires education and persuasion. To achieve this objective, the following four thrust areas were identified to see that boards could effectively deliver. These includes :

- Roles and Responsibilites of Boards
- Independence of the Boards
- Composition of the Boards
- Commitment of the Boards

## Chapter 5: Comparison of Duties of Directors

*The chapter 5 deals with the comparison of regulatory agencies, corporate governance principles, number of committees, duties of directors across the boards and case studies. Further the chapter provides conclusions and recommendations.*

The role of Boards is to guard the company and to improve the governance standards. Table 1 depicts the regulators responsible for implementing Corporate Governance practices in the countries of study. In India, Securities and Exchange Board of India and Ministry of Corporate Affairs together are responsible in designing the code of corporate governance mandating to be followed by all the listed companies. Whereas, Securities and Exchange Commission for USA, Financial Conduct Authority for UK, Australian Securities and Investment Commission for Australia, Monetary Authority of Singapore for Singapore, and Securities Commissions for Malaysia.

**Table 5.1: Main Public regulators of Corporate Governance**

Sl No.	Jurisdictions	Key Regulators	
1	India	SEBI	Securities and Exchange Board of India
		MCA	Ministry of Corporate Affairs
2	United States	SEC	Securities and Exchange Commission
3	United Kingdom	FCA	Financial Conduct Authority
4	Australia	ASIC	Australian Securities and Investment Commission

Sl No.	Jurisdictions	Key Regulators	
5	Singapore	MAS	Monetary Authority of Singapore
6	Malaysia	SC	Securities Commission

Source : Compiled OECD guidelines on Corporate Governance of State Owned Enterprises Handbook, 2015

Table 5.2 depicts the budgets and funding of regulators of corporate governance. The most of the funding is allocated in the national budget whereas, approvals were obtained from the government agencies such as Ministry of Finance, Ministry of Corporate Affairs, etc in all the countries referred in the study. In the case of United States, the SEC receives fees from regulated entities but Congress determines the SEC's funding.

**Table 5.2: Budget and Funding of Main Regulators of Corporate Governance**

Sl.No.	Jurisdictions	Form of Funding	Main Funding Resources	Budget approved by	
			National Budget (NB)	Government (Ministry of Finance, etc.,)	Congress
1	India	Public & Self	Yes	-	-
2	United States	Public	Yes	Required	Required
3	United kingdom	Self	-	Required	Required
4	Australia	Public	Yes	-	-
5	Singapore	Self	Yes	-	-
6	Malaysia	Public	Yes	-	-

Source : Compiled OECD guidelines on Corporate Governance of State Owned Enterprises Handbook, 2015

The ruling bodies of CG regulators Table 5.3 depicts that most of the regulators have boards whereas USA, Australia and Malaysia has Commissions. The members of regulatory boards

range between 5 and 9. In the case of USA the commission should not have more than 3 members for the same party. Table 3 depicts the ruling bodies and members of the regulators.

**Table 5.3: Ruling bodies of Corporate Governance Regulators**

Jurisdictions	Key Regulators	Ruling body in charge of Corporate Governance	Members incl. chair (current)	Representatives from specific entity				Appointments
				Government	Central Bank	Others Public	Others private	
India	SEBI / MCA	Board	9	Yes	Yes	-	-	Ministry of Finance
United States	SEC	Commission	5	Yes	-	-	-	President
United kingdom	FCA	Board	12	Yes	-	Yes	-	Treasury
Australia	ASIC	Commission	3-8 (5)	-	-	-	-	Government –General
Singapore	MAS	Board of Directors	9	-	-	-	-	President
Malaysia	SC	Commission	d	Yes				Ministry of Finance

Source : Compiled OECD guidelines on Corporate Governance of State Owned Enterprises Handbook, 2015

**Table 5.4: Terms and appointment of the ruling body of main regulators of Corporate Governance**

<b>Jurisdiction</b>	<b>Key Regulators</b>	<b>Ruling body in charge of Corporate Governance</b>	<b>Term</b>	<b>Re-appointment</b>	<b>Appointment by:</b>	<b>Approval by Parliament</b>
India	SEBI	The Board		Ministry of Finance		
	MCA					
United kingdom	FCA	Board	3	Allowed	HM Treasury, Department for Business Innovation and Skills	Not Required
United States	SEC	Commission	5		President	Required
Singapore	MAS	Board of Directors		President		

Source : Compiled OECD guidelines on Corporate Governance of State Owned Enterprises Handbook, 2015

The legal framework of corporate governance is governed by the guidelines from the regulatory agencies. Table 5.5 gives an overview of the company's law, securities law and other regulations that are governing the corporate governance. Countries such as Malaysia and Singapore have been following the code of corporate governance. Other countries have amended the law as per the requirements.

**Table 5.5: Regulatory framework - Laws and Regulations**

<b>Jurisdictions</b>	<b>Companies Law</b>	<b>Securities Law</b>	<b>Other relevant regulations on corporate governance</b>
India	Companies Law 2013	Securities and Exchange Board of India Act	Listing Agreement – Clause 49

<b>Jurisdictions</b>	<b>Companies Law</b>	<b>Securities Law</b>	<b>Other relevant regulations on corporate governance</b>
United States	State Corporate Laws	The Securities Act of 1993 The Exchange Act of 1934	
United kingdom	Companies Act, 2006	Financial Services and Market Act 2000	Listing Rules, Prospectus rules, Disclosure and Transparency Rules (FCA)
Australia	Corporation Act 2001	-	-
Singapore	Companies Act	Securities and Future Act	
Malaysia	MCG code 2001		

Source : Compiled OECD guidelines on Corporate Governance of State Owned Enterprises Handbook, 2015

### **Duties of Directors**

Fiduciary duties of the board are analyzed by considering three basic parameters. These include loyalty towards organization, time taken for response and the disclosure mechanisms.

**Table 5.6: Fiduciary Duties of the Directors**

<b>Jurisdictions</b>	<b>Loyalty</b>	<b>Action</b>	<b>Disclosure</b>
India	Ensure and secure the interest of the company	Timely and swift resolutions	Mandated to disclose the information to all stakeholders as per listing agreement

<b>Jurisdictions</b>	<b>Loyalty</b>	<b>Action</b>	<b>Disclosure</b>
United States	Fair process	business judgment rule	disclose all material information by shareholders
United kingdom	Transparency	Judicial framework	Disclosure as per the guidelines
Australia	Equitable obligations	Good faith and not to act contrary to the interest of the company	Disclosure as per the guidelines
Singapore			Disclosure as per the guidelines
Malaysia	Ethical Values and standards	Stakeholders interest	Board charter in annual reports delineate the roles

Source : Authors compilation

Board and board committees are broadly classified as governance control and internal control. The governance controls are further divided into audit committee, nomination committee and remuneration committee. The internal control system has risk management committee. The audit committee is headed by an independent director in all the countries under reference. The composition of independent directors in the audit committee is 100 per cent in the case of US and UK. Whereas, India holds at 66 per cent and Australia, Malaysia and Singapore composes 50 per cent independent directors as members in audit committees.

**Table 5.7: Board and Board Committees (mandated as per Law)**

Jurisdictions	Board Level Committees			
	Governance Control			Internal Control
	Audit Committee	Nomination Committee	Remuneration Committee	Risk Management
India	Law and regulation	As per the code of CG	As per the code of CG	As per the code of CG
United States	Law and regulation	Law and regulation	As per the code of CG	As per the code of CG / Listing agreement
United Kingdom	As per the code of CG	As per the code of CG	As per the code of CG	As per the code of CG
Australia	As per the code of CG	As per the code of CG	As per the code of CG	As per the code of CG
Singapore	Law and regulation	As per the code of CG	As per the code of CG	As per the code of CG
Malaysia	As per the code of CG	As per the code of CG	As per the code of CG	As per the code of CG

Source : Authors compilation

### **Duties of the Boards of Directors**

Table 5.8 discusses the role and functions of various committees that are mandated by the corporate governance codes. Audit committee, nomination committee and remuneration committee are three major committees which are formed by all the countries as a part of the governance control. The committees have an independent director as chairman. In UK, the



risk management committee is named as board enterprise wide risk management. The functions of the committee are similar to the functions of the risk management committee. The committee is responsible for maintaining the internal controls in the corporation. In India we have CSR Committee as a mandated committee for all the listed enterprises. The committee is responsible for all the CSR activities that are undertaken by the corporation. The committee is headed by an independent director.

**Table 5.8 : Board Level Committees**

<b>Jurisdictions</b>	<b>Governance Control</b>			<b>Internal Control</b>	
	<b>Audit Committee</b>	<b>Nomination Committee</b>	<b>Remuneration Committee</b>	<b>Risk Management</b>	<b>Other Committees</b>
United States	Yes	Yes	Yes	Yes	
United Kingdom	Yes	Yes	Yes	Board Enterprise Wide Risk Committee	
Australia	Yes	Yes	Yes	Yes	-
Singapore	Yes	Yes	Yes	Yes	Executive Committee
Malaysia	Yes	Yes	Yes	Yes	Committee Shareholders
India	Yes	Yes	Yes	Yes	Shareholders Committee, CSR Committee,

Source : Authors compilation

Table 5.9 depicts the general duties of the board. The board's primary function is to manage and supervise the business to achieve the organizational objectives. Singapore boards provide entrepreneurial leadership; sets core values and standards and prioritize sustainability issues such as environmental and social factors. Australian boards follow the

general duties that no board member should use the information obtained through position to gain an advantage for self or someone else. Indian boards do not lay down all the duties of the boards specifically but, tries to integrate with the regulators as the duties are mandatory for board members of listed enterprises. In the case of Australia all listed companies should have and disclose a *board skills matrix* setting out the mix of skills and diversity that the board currently has or is looking to achieve. The boards “skills matrix” is useful tool that can help to identify any gaps in the collective skills of the board that should be addressed as part of a listed entity’s professional development initiatives for directors and in its board succession planning. This kind of matrix is not available in any country. USA and Singapore are evaluating the performance of boards. India is also working on board evaluation for it public sector enterprise.

**Table 5.9: General Duties of the Board**

<b>USA</b>	<b>UK</b>	<b>Australia</b>	<b>Singapore</b>	<b>Malaysia</b>	<b>India</b>
<ul style="list-style-type: none"> <li>• Manage Business</li> <li>• Strategic objectives</li> <li>• Financial planning and control</li> <li>• Conduct elections</li> <li>• Compliance</li> </ul>	<ul style="list-style-type: none"> <li>• act within powers</li> <li>• promote the success of the entity</li> <li>• exercise independent judgment</li> <li>• reasonable care, skill and diligence</li> <li>• avoid conflicts of interest</li> </ul>	<ul style="list-style-type: none"> <li>• exercise powers and duties with the care and diligence</li> <li>• ensure to share financial information</li> <li>• to exercise powers and duties in good faith</li> <li>• not to improperly use position to gain an advantage</li> <li>• not to use information</li> </ul>	<ul style="list-style-type: none"> <li>• provide entrepreneurial leadership, set strategic objectives,</li> <li>• establish framework of prudent and effective controls</li> <li>• review management performance;</li> <li>• identify the key stakeholder groups and recognise that their perceptions</li> <li>• set the company's values and standards</li> <li>• consider sustainability issues, e.g. environmental</li> </ul>	<ul style="list-style-type: none"> <li>• establish clear roles and responsibilities</li> <li>• strengthen composition</li> <li>• reinforce independence</li> <li>• foster commitment</li> <li>• uphold integrity in financial reporting</li> <li>• recognize and manage risks</li> </ul>	<ul style="list-style-type: none"> <li>• to exercise duties as per the regulations of the articles of association</li> <li>• valid if the resolution to be passed</li> <li>• approve financial statement</li> <li>• enhance and diversify the business opportunities</li> </ul>

USA	UK	Australia	Singapore	Malaysia	India
		<p>obtained through your position to gain an advantage for self or someone else, or to cause detriment to the company</p> <ul style="list-style-type: none"> <li>• not trade while insolvent</li> </ul>	and social factors		

Source : Authors compilation

Table 5.10 details about the duties and responsibilities of the board committees. Audit committee has been one of the prime committee that is mandated all the countries. The following are the duties of audit committees of the countries referred in the study.

**Table 5.10: Duties and Responsibilities of the Audit Committees**

<b>Jurisdictions</b>	<b>Audit Committees</b>	<b>Nomination Committees</b>
United States	<ul style="list-style-type: none"> <li>• discussing on the internal accounting procedures</li> <li>• recommend board reading nomination of external auditors to be appointed by the shareholders</li> <li>• to discuss the audit procedures</li> <li>• regularly informing the board important findings of the audit results</li> <li>• oversee the quality of internal and external auditing</li> <li>• review reports regarding internal controls and risk assessment at the organization</li> </ul>	<ul style="list-style-type: none"> <li>• Identifying, assessing and recommending to the Board candidates for appointment of Directors</li> <li>• Making recommendations on policy on the term of appointment</li> <li>• Making recommendations to the Board on the composition of Committees</li> <li>• Reviewing regularly the structure, size and composition of the Board</li> <li>• Reviewing proposals for changes in responsibilities of Board members.</li> <li>• Making recommendations to the Board concerning any matter relating to the continuation in office of any Director at any time.</li> </ul>

<b>Jurisdictions</b>	<b>Audit Committees</b>	<b>Nomination Committees</b>
		<ul style="list-style-type: none"> <li>• Reviewing at least annually succession planning both to the Board and to the senior management grade immediately below Board level.</li> </ul>
United Kingdom	<ul style="list-style-type: none"> <li>• Assessing the integrity of financial reporting and satisfying significant financial judgments</li> <li>• Evaluating the effectiveness of internal controls, including internal financial controls; and</li> <li>• Scrutinizing the activities and performance of the internal and external auditors, including monitoring their independence and objectivity.</li> </ul>	<ul style="list-style-type: none"> <li>• Support and advise the Board in ensuring that the composition of the Board and its Committees is appropriate and enables them to function effectively;</li> <li>• Examine the skills, experience and diversity on the Board and plan succession for key Board appointments, planning ahead to deal with upcoming retirements and to fill any expected skills gaps;</li> <li>• Provide oversight of the management programme and diversity and inclusion initiatives;</li> <li>• Agree the annual Board effectiveness review process and monitor the progress of any actions arising</li> </ul>
Australia	<ul style="list-style-type: none"> <li>• the adequacy of the entity's corporate reporting processes;</li> <li>• whether the entity's financial</li> </ul>	<ul style="list-style-type: none"> <li>• board succession planning generally;</li> <li>• induction and continuing</li> </ul>

Jurisdictions	Audit Committees	Nomination Committees
	<p>statements reflect the understanding of the committee members of, and otherwise provide a true and fair view of, the financial position and performance of the entity;</p> <ul style="list-style-type: none"> <li>• the appropriateness of the accounting judgements or choices exercised by management in preparing the entity's financial statements;</li> <li>• the appointment or removal of the external auditor;</li> <li>• the rotation of the audit engagement partner;</li> <li>• the scope and adequacy of the external audit;</li> <li>• the independence and performance of the external auditor;</li> <li>• any proposal for the external auditor to provide non-audit services and whether it might compromise the independence of the external auditor</li> </ul>	<p>professional development programs for directors;</p> <ul style="list-style-type: none"> <li>• the development and implementation of a process for evaluating the performance of the board, its committees and directors;</li> <li>• the process for recruiting a new director, including evaluating the balance of skills, knowledge, experience, independence and diversity on the board and, in the light of this evaluation, preparing a description of the role and capabilities required for a particular appointment;</li> <li>• the appointment and re-election of directors; and</li> <li>• ensuring there are plans in place to manage the succession of the CEO and other senior executives.</li> </ul>
Singapore	<ul style="list-style-type: none"> <li>• to ensure the integrity of the financial statements of the company performance</li> </ul>	<ul style="list-style-type: none"> <li>• To plans for board succession and ensures that they are capable of contributing to the success of</li> </ul>

<b>Jurisdictions</b>	<b>Audit Committees</b>	<b>Nomination Committees</b>
	<ul style="list-style-type: none"> <li>• reviewing and reporting to the Board at least annually the adequacy and effectiveness of the company's internal controls, including financial, operational, compliance and information technology controls (such review can be carried out internally or with the assistance of any competent third parties)</li> <li>• reviewing the effectiveness of internal audit function</li> <li>• reviewing the scope and results of the external audit</li> <li>• making recommendations to the Board on the proposals to the shareholders on the appointment</li> </ul>	<p>the organization are appointed.</p> <ul style="list-style-type: none"> <li>• Reviews all nominations for the appointment, re-appointment, election or re-election of Directors</li> <li>• Determines annually whether or not a Director is independent and qualified</li> <li>• It also reviews nominations for senior management positions</li> </ul>
Malaysia	<ul style="list-style-type: none"> <li>• financial statements comply with applicable financial reporting standards</li> <li>• policies and procedures to assess the suitability and independence of external auditors</li> </ul>	-
India	<ul style="list-style-type: none"> <li>• Oversight of the company's financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct,</li> </ul>	<ul style="list-style-type: none"> <li>• Identify persons who may be appointed as directors and senior management, and recommend to board appointment and removal of director and evaluate</li> </ul>



<b>Jurisdictions</b>	<b>Audit Committees</b>	<b>Nomination Committees</b>
	<p>sufficient and credible.</p> <ul style="list-style-type: none"> <li>• Recommending to the Board, the appointment, re-appointment and, if required, the replacement or removal of the statutory auditor and the fixation of audit fees.</li> <li>• Approval of payment to statutory auditors for any other services rendered by the statutory auditors.</li> <li>• Reviewing, with the management, the annual financial statements before submission to the board for approval, with particular reference to:</li> <li>• Matters required to be included in the Director's Responsibility Statement to be included in the Board's report in terms of clause (2AA) of section 217 of the Companies Act, 1956</li> <li>• Changes, if any, in accounting policies and practices and reasons for the same</li> <li>• Major accounting entries involving estimates based on the</li> </ul>	<p>performance of directors.</p> <ul style="list-style-type: none"> <li>• Committee to formulated criteria for determining qualifications, attributes and independence of director and recommend to board policy regarding remuneration of directors, key managerial personnel and other employees.</li> <li>• While formulating policy committee should ensure following:-</li> <li>• Level and remuneration to directors should be sufficient to attract, retain &amp; motivate directors of quality</li> <li>• Relationship of remuneration to performance is clear and meets appropriate performance benchmarks</li> <li>• Remuneration to Directors and senior management involves a balance between fixed and incentives reflecting performance</li> </ul>

Jurisdictions	Audit Committees	Nomination Committees
	<p>exercise of judgment by management</p> <ul style="list-style-type: none"> <li>• Significant adjustments made in the financial statements arising out of audit findings</li> <li>• Compliance with listing and other legal requirements relating to financial statements</li> <li>• Disclosure of any related party transactions</li> <li>• Qualifications in the draft audit report</li> <li>• Reviewing, with the management, the quarterly financial statements before submission to the board for approval</li> <li>• Reviewing, with the management, the statement of uses / application of funds raised through an issue</li> </ul>	

Source : Authors compilation

Table 5.11 depicts the Country-wise Case Study of the Board Committees. The duties of directors of the various board committees such as audit, nomination, remuneration or compensation, corporate governance, risk management, CSR and other committees are discussed. It is observed that audit, nomination, remuneration or compensation committees are mandated by all the companies that are referred in the study.

**Table 5.11: Country-wise Case Study of the Board Committees**

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
USA (Nestle Ltd – AR 2015 )	<b>Chairperson</b> – ID & NED’s  <b>Existing</b> - four members	- discuss internal accounting procedures  - read nominations of external auditors to be appointed by shareholders  - discuss audit procedures  - Regularly informing board important finding of	<b>Chairperson</b> – ID  <b>Existing</b> - four members	- Principles for selection of candidate to boards and conduct elections  - Annually review the independence of the board & their outside mandates  - Prepares annual self evaluation of board & its committees	<b>Chairperson</b> – Vice Chairman & Min. 2 NED (all ID)  <b>Existing</b> - four members	- Determine principle remuneration of chairman, CEO, & individual Board Member  - Prepare proposal for AGM’s in relation to compensation issues	<b>Chairperson</b> – Vice Chairman & CEO Members elected by chair  <b>Existing</b> - four members	- Reviews CG practice  - Prepare recommendations for implementation  - Advices on finance related matters including financial performance, financial management  - Review of						

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
		audit results - O - oversee the quality of internal and external auditing - R - review reports regarding internal control and risk assessment						assets and liabilities						
UK (British Petroleum)	<i>Chairperson – ID Existing – 05 members</i>	– Monitors the effectiveness of the group's financial reporting, systems of internal	<i>Chairperson – Chairman of Company Existing – 07 members</i>	- Identify, evaluate and recommend candidates for appointment or reappointment	<i>Chairperson – Existing – 06 members</i>	- Determine remuneration policy for all directors - Prepare annual report to shareholders about implementation of policy		-	,				Safety, ethics and environment assurance Committee (SEE	SEEAC mitigate significant non-financial Risk monitoring the management of personal and process

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
		control and risk management and the integrity of the group's external and internal audit processes . - Review financial statements and other financial disclosures - Overseeing integrity of auditors and appointments of external		as directors. - Identify , evaluate and recommend candidates for appointment as company secretary. - Keep under review the mix of knowledge, skills and experience of the board to ensure the		- Approve the principles of any equity plan for which shareholder approval is to be sought. - Approve, monitor the terms of remuneration for executives, group leaders etc -							AC) Chair person - ID Existing – 07 members  Gulf Committee <i>Chair person</i> - ID Existing – 05	safety and receiving assurance that processes to identify and mitigate such non-financial risk are appropriate in design and effective in implementation  - oversee the management and mitigation of legal and license to operate risks arising out of the

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
		auditors		orderly succession of directors. - Review the outside directorship/commitments of non-executive directors.									members	Deepwater Horizon accident and oil spill. -Review the environmental work to remediate or mitigate the effects of the oil spill Oversee management strategy and actions to restore the group's reputation
Singapore (OCBC Bank – AR)	<b>Chairperson</b> - ID, 02 <b>members</b> – ID	– review group financial statements – R	<b>Chairperson</b> – ID <b>Existing</b> – 05	– reinforcing the principles of transparency and meritocracy at the Bank	<b>Chairperson</b> – ID <b>Existing</b> –	– recommends to the Board a framework for determining the		–	<b>Chairperson</b> – ID <b>One NED Existing</b> –	– reviews the overall risk management			<b>Executive Committee</b> <b>Chair</b>	– Oversees management of business – Bank's

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
2015 )	<b>Existing</b> – three members (all are ID's)	reviews and evaluates with the external auditors and internal auditors – reviews the scope and results of the audits, the cost effectiveness of the audits, and the independence and objectivity of the external auditors	<b>Members</b>	– appointment of board of directors – review of all nominations for the appointment, election or re-election as well as resignations of directors –	<b>05 members (all are ID's)</b>	remuneration of executive officers – reviews remuneration practices – empowered to review the human resources management policies and the policies governing the compensation of executive officers			<b>06 members</b>	philosophy, guidelines and major policies for effective risk management – reviews the scope, effectiveness and objectivity of Group Risk Management and the risk reports – identifying, measuring, monitoring, controlling			<b>Members</b> – Chairman of the company and all members are ID	policies, principles, strategies, values, objectives and performance targets

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
										g and reporting risks on an enterprise-wide basis, including ensuring the adequacy of risk management practices for material risk				
Australia (Sun crop Group Ltd)	<i>Chair Person – ID Existing – four ID</i>	– Reviewing statutory reports and returns for lodgment with APRA – Reviewing half-year and	<i>Chair person – Chair man of the Company</i>	– Making recommendation to board on Board composition, board renewal & succession plan – Appointment and re-	<i>Chair Person – ID Existing – four members (*all ID's)</i>	– Recommendation on individual remunerations of Board of Directors – size of the annual bonus/ incentive pools – rem		–	<i>Chair Person – ID Existing – five members (*all ID's)</i>	– Review and recommend for Board approval the Enterprise Risk Management Framework				-



Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
		annual financial statements and reports prior to consideration by the Board – Review and assess reports from management, external auditors, Appointed Actuary etc – Reviewing and approving audit plans – Reviewing the provision		appointment of directors and appointments of Board committees – Board and individual director and committee performance evaluation process –		Remuneration structure of the categories of persons covered by the Company's remuneration policy				– Review Group and line of business risk reports and assess performance against risk appetite – Review and approve stress test scenarios – Review and recommend risk management strategies and reinsurance				

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
		of non-audit services by the external auditor to assess the potential impact of auditor's independence – Reviewing internal and external audit reports								management strategies as required by APRA – enables business risk based decision-making.				
Malaysia (May Bank Ltd)	<b>Chair Person – ID Existing – 04 members (*all memb</b>	– To review and assess internal audit reports – To review and assess the performance of	Chair person – ID All members are NED's <b>Existing -</b>	- To recommend the appointment, promotion and remuneration as well as compensation policies		–		–	<b>Chair person – Existing -</b>	– To review and approve risk management strategies, risk frameworks, risk policies, risk			Credit review committee	- review/verify loans exceeding the Group Management Credit Committee discretionary power - review/verify

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
	<i>er are ID)</i>	internal and external auditors – To review the appointment, termination and resignation of the external auditors and its audit fees – To review the quarterly results and year-end financial statements focusing particularly on the reliability of the		for executives in key management positions - Recommend Leadership Development framework - To oversee the selection of Directors and general composition of Board - assess the performance and						tolerance and risk appetite limits - To identify, measure, monitor and control risks and the extent to which they operate effectively - To ensure infrastructure, resources and systems are in place for risk management - To				o, with power to object or support, all proposals recommended by the GMCC to the Board for approval/affirmation - provide oversight of the entire credit management function covering but not limited to portfolio, end-to-end process, infrastructure

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
		information disclosed therein, changes in accounting policy, significant and unusual events as well as compliance with accounting standards and other legal requirements –		effectiveness of individuals and collective members of the Boards and Committees - To oversee the succession planning, talent management and performance evaluation of executives in key management position						review management's periodic reports on risk exposure, risk portfolio composition and risk management activities				ure, resources and governance

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
India (TATA Steel)	<b>Chairperson – ID Existing – 05 members</b>	– to monitor and provide an effective supervision of the Management’s financial reporting process – to ensure accurate and timely disclosures, with the highest levels of transparency, integrity and quality of financial reporting – to oversee	Chairperson – ID Existing – four members	– to oversee the Company’s nomination process for the senior management – to identify, screen and review individuals qualified to serve as EDs, NEDs and IDs consistent with criteria approved by the Board and to recommend – to assess the compensation of the Company’s EDs and senior management – To approve and		–		–	<b>Chairperson – ID Existing – nine members</b>	– Overseeing key risks, including strategic, financial, operational and compliance risks. – Assisting the Board in framing, implementing and monitoring the risk management plan for the Company and reviewing and guiding the risk policy. – Developing risk	Chairperson – NED Existing – five directors	– to formulate and recommend to the Board, a Corporate Social Responsibility Policy, which shall indicate the activities to be undertaken by the Company – to recom	Stakeholders’ Relationship Committee	– to consider and resolve the grievances of the security holders –

Country / Company	Audit Committee		Nomination Committee		Remuneration / Compensation Committee		Corporate Governance Committee		Risk Management Committee		CSR Committee		Other Committees	
	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties	Composition	Duties
		the work carried out in the financial reporting process by the Management, the internal auditor, the statutory auditor and the cost auditor		evaluate the compensation plans, policies and programmes for EDs and the senior management – To coordinate and oversee the annual self-evaluation of the performance of the Board, Committees' and of individual Directors						management policy and risk management system/framework for the Company		monitor the amount of expenditure to be incurred on CSR activities - monitor from time to time the CSR Policy of the Company		

(Source : Data extracted from the company's annual reports for the year 2015)

Note : \* *Nomination committee and Remuneration Committee of Maybank Ltd, Malaysian and TATA Steel, India companies committees are combined together and the committee formed is stated as Nomination and Remuneration Committee. The duties of the committee are given in the above table.*

*Depending on the business of the companies different types of committees are being formed but in most cases these are focused committees which are common and mandated by the company's respective laws and acts.*

## Conclusions and Recommendations

The conclusions and recommendations are discussed in two parts. Part1,the theory of corporate governance and secondly, the duties of directors.

All these steps are corporate governance practices applied not by sitting in a boardroom receiving information from the management, but through active governance essential to monitoring the company. The boards must lead by setting up systems to monitor the compliance by the company with legal standards and regulatory requirements. Heading the committee would be an independent non-executive director with experience in monitoring and establishing internal control procedures. The board should always make sure it has a full understanding of the business structure and model in order to govern and monitor it effectively. Where it does not, the board must take *proactive* measures to gain a full understanding of the business. The board evaluations establish for the purpose of assessing areas of possible improvement by measuring the board in relation to the corporate strategies or the vision set out by the board. The evaluation is to be taken seriously, with directors and management open about critiquing and stating the deficiencies of expertise or problems on the board.

In general, there are three types of board ; a board that creates negative value (deteriorates the company from its earlier position); a board that creates no value (ensures compliance and maintains the status quo); or a board that creates value (through vision and strategic guidance). Every board desires and strives to be a “value creator.” They all want to live up to the expectations. They want to create great companies, companies. As the boards with stronger character and ability to do things differently or board with a vibrant personality, a 360-degree view capable of taking complex decisions in trying situations and making sure that those decisions are implemented. As discussed earlier, such a board needs to be made of members

who are heterogeneous in terms of personality gender, age, race, nationality, education, and experience. Board diversity is a very important area for enhancing board performance. Succession planning board succession planning process must be put in place, whereby through an aggressive recruitment process top-quality members are selected based on the current and future needs.

The theory of corporate governance does define the general duties of boards and board committee. The Corporate entities try to draw the framework basing on the nature and economic activity of the corporations. The general duties of directors are similar to arguments in favor of non-uniform duties that are been prioritized rather than the uniform duties. However, restrictions imposed by law may not matter. Every business should be fair and should not suffer from the preference given to the standard duty strategy. The strong legal framework prevailing in every country tries to protect the interest of the shareholder. Legal and regulatory framework deals with a dual reality as they enable the corporation to develop and evolve. They are keen on selecting rules that they enforce more diligently than others. The duty of confidentiality, which is relatively strict in monitoring the area of corporate governance, mandates the directors' duties into the legal regime. For example, the shareholder primacy norm in the US is generally not considered to be enforced with any vigor. The main conflict of interest between shareholders and creditors is of high risk situations and boards need to act to protect the interest of the stakeholders. The study highlights the non-uniform duties of the boards and board committees seem more persuasive than those in favor of uniform duties. The UK corporate governance process followed 'comply or explain' mode of governance system for its entities. The job of monitoring the board has largely fallen to the standard audit committee in recent years. Internal controls are an important duty of the boards as risk management, effectiveness of compliance



and the ability of the company to deal with sudden circumstances. The board needs to focus on pre-empting potential to fix problems and restoring trust in a company.

The Malaysian Corporate Governance (CG) policy focus on, a strong foundation for the board and its committees to carry out their roles effectively, promote timely and balanced disclosure, safeguard the integrity of financial reporting, emphasize the importance of risk management and internal controls and encourage shareholder participation in general meetings. The countries Securities Exchange Commissions plays key role in monitoring the duties of directors and regulating them from time to time. Australian boards follow the guidelines laid down by the Companies Act 2001. Indian Companies Act, 2013 has considered bring all the various issues of the board benchmarking them with international standards. The code of corporate governance mandates all listed public enterprise to comply with the standards.

All the countries have the governance controls mandated by code of corporate governance. The respective committee has defined its duties and noted in the corporate governance code. Hence, the companies follow these guidelines, in line with the code and act on the duties as they have to be complying with the norms.

Ultimately, it is important to understand that potential board member must aim must to have a broad talent base. There is no ideal mix of directors: It depends on the needs of the company and its business. It is important to understand the talents and skills that will be needed in the future and plan accordingly. The duties of directors, board talent must be strategically managed to build a competent board with diverse perspectives and skills. To enhance board performance and create value that diverse boards can generate, members need to recognize the diversities,

appreciate and respect the diversities, learn to work as a team, irrespective of diversity and leverage the diversity. To conclude, board duties provides key to the board effectiveness. The boards suffer from inadequacy which is truer in the case of the PEs in India.

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