ANALYSING CORPORATE GOVERNANCE AND CORPORATE FINANCE IN INDIA IN LIGHT OF THE COMPANIES ACT, 2013

Simran Sethi, Guru Gobind Singh Indraprastha University, Dwarka.

ABSTRACT

Corporate governance and corporate finance serve as the cornerstones for the overall functioning and growth of companies particularly within the emerging markets like India. The Companies Act, 2013 bought significant reform in India's legal framework governing corporate entities in India. The paper analyses the efficacy of these statutory reforms in fostering a stronger and more resilient corporate sector in India, while also acknowledging the challenges in enforcement and implementation. This paper discusses the intersection of corporate governance and corporate finance as shaped by the provisions of the Companies Act, 2013 in order to analyze the impact on board structures, accountability, financial reporting and financial management.

The study concludes that while the Act has fostered a more investor-friendly ecosystem conducive to long-term economic growth, continuous legislative amendments and vigilant regulatory oversight remain essential to navigate India's evolving business landscape.

Keywords: Corporate Governance, Corporate Finance, Companies Act, 2013, Board of Directors, Financial Reporting, Accountability, Transparency, Shareholders Rights.

1. Introduction

Corporate governance refers to set of rules, practices and processes by which a company is directed and controlled. It refers to the mechanisms through which the various stakeholders including shareholders, board of directors, managers are held accountable. Corporate Finance on the other hand, involves the management of financial resources in a way that maximizes shareholder value while maintaining financial stability.

The Companies Act, 2013, was enacted by the Indian Government with the objective of improving corporate governance and aligning India's regulatory framework with international best practices. The Act aims to address the shortcomings in the prior Companies Act of 1956, which became outdated and ineffective in dealing with modern day corporate frauds, mismanagement and other financial challenges.

This paper discusses the intersection of corporate governance and corporate finance as shaped by the provisions of the Companies Act, 2013 in order to analyze the impact on board structures, accountability, financial reporting and financial management.[1]

2. Overview of the Companies Act, 2013

The Companies Act, 2013 is a comprehensive legislation which governs the incorporation, regulation and dissolution of companies in India. It came into force on April 1, 2014 and replaced the Companies Act of 1956. The Act consists of 29 chapters and 470 sections covering a wide array of issues including financial disclosures, mergers, corporate governance and Corporate Social Responsibility (CSR).

Some of the key components of the Act are as follows:

- **Financial Reporting and Accountability:** the Act consists of enhanced provisions or financial disclosures, audit requirements and regulatory oversight of financial statements.
- **Stakeholders Protection:** the act includes clear provisions with respect to

[1] S. Khurana & S. Khanna, *Corporate Governance in India: A Review of the Companies Act, 2013*, 4 Asian J. Bus. Ethics 211 (2015).

minority shareholder rights and regulation of related party transactions.

- **Strengthens Corporate Governance**: the act mandates a transparent and accountable structure for companies with specific rules about board composition, duties of directors etc. [2]

3. Corporate Governance in context of the Companies Act, 2013

Corporate Governance in India has significantly evolved over the years. The Act strengthens governance practices by implementing several reforms aimed at transparency, accountability, responsibility and fairness, which in turn form the four fundamental principles of corporate governance.[3]

The key provisions which strengthens and ensure corporate governance under the Act include the following:[4]

3.1. Board of Directors

1) **Section 149- Composition of Board:**

   - Every company (except for One Person Company) must have a Board of Directors.
   - Public companies must have at least three directors, while a private company needs a minimum of two.
   - The board should have a minimum of one-third independent directors in certain cases such as for listed companies and other prescribed categories.
   - The company must appoint a woman director if it is a listed company or falls under the prescribed categories.

2) **Section 152- Appointment of Directors:** The directors are appointed through a process specified in Articles of Association (AOA) and by shareholder approval

[2] The Companies Act, 2013, No. 18, Acts of Parliament, 2013 (India).
[3] Indian Inst. of Corp. Affairs, Corporate Governance in India: Legal and Regulatory Overview (2014).
[4] R. Singh & M. Gupta, *Corporate Finance and Governance: Analyzing Key Provisions under the Companies Act, 2013*, 22 J. Bus. L. & Ethics 113 (2017).

at the AGM.

3) S**ection 161- Appointment of Additional and Alternate Directors:** the board can appoint additional director and alternate director to act in place of a director who is absent for a specified period.

4) **Section 167- Vacation of Office of Director:** specifies grounds for vacation of office, including if director becomes disqualified or fails to attend meetings. [5]

3.2. Independent Directors: The Act mandates the appointment of **Independent Directors (IDs)** in certain categories of public companies to ensure objectivity in decision-making. While **Section 149(6)** of the Act defines criteria for being an independent director, **Section 149(7)** mandates submission of declaration of independence by the independent director to the board in order to confirm that they meet the requirements as specified.

3.3. Provision for Audit Committee (Section 177): Every listed company and certain public companies are mandated under the Act to establish Audit Committee consisting of non-executive directors with the majority being independent directors. The committee is responsible for recommending the appointment, remuneration and terms of appointment of the Auditors. They are responsible to examine the financial statement, auditors report, etc.

3.4. Nomination and Remuneration Committee (section 178): Every listed company and certain other prescribed public companies must have a nomination and remuneration committee responsible for recommending the appointment and remuneration of directors and senior management, including setting the terms of employment, performance evaluation etc.

3.5. Disclosure of Interest by Directors (Section 184): This section mandates directors of the company to disclose their interest in the company as well as in any contract or arrangement in which they have a direct or indirect interest. The company must maintain a register of interests in which all such declarations are recorded. [6]

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[5] *id.*

[6] S. Verma & M. Kumar, *Impact of the Companies Act, 2013 on Corporate Governance in India*, 9 Indian J. Corp.

3.6. Corporate Social Responsibility (CSR) (Section 135): certain companies are required to contribute a certain percentage of their net profit towards social activities. The CSR Committee frames policies and strategies for CSR Initiatives and a report on the same is included in Board's report. [7]

3.7. Shareholder Rights and Protection: The Act consists of various provisions that ensure that rights of the shareholders are protected which in turn strengthens corporate governance framework in India.[8] This include the following:

1) **Right to Receive Information:** shareholders are entitled to receive notice of meetings in writing or by electronic means, at least 21 days before the date of meeting (**Section 101**). Shareholders also have the right to access minutes of the meeting (**Section 118**) and have the right to inspect about the company's financial statements. (**Section 129**)

2) **Right to Vote:** shareholders are entitled to vote on resolutions, including special resolutions. The vote can be casted by postal ballot, e-voting or in person at the AGM. (**Section 110**).

3) **Protection from Oppressive or Prejudicial Actions:** shareholders including minority shareholders have a right to file application before National Company Law Tribunal (NCLT) if they feel that affairs of the company are being conducted in a manner oppressive or prejudicial to their interests. (**Section 241-242**). Further committing fraud is punishable under **Section 447** of the Act.

4) **Right to Transfer Shares:** Subject to limitations imposed by private companies, the shareholders have a right to transfer their shares in accordance with the law. (**Section 56**).

5) **Right to Approve Key Corporate Decisions:** certain decisions such as borrowing beyond a certain limit require approval from the shareholders through a special resolution at the AGM or EGM. This ensures that shareholders have the right to make decisions which significantly impact company' financial direction. (**Section 180-**

Gov. 14 (2016).

[7] M.K. Nandakumar & S. Mookerjee, *Corporate Social Responsibility in India: Exploring the Impact of the 2013 CSR Law*, 15 Asian Bus. & Mgmt. 191 (2016).

[8] R. Bhatia, *Shareholder Rights and Protection under the Companies Act, 2013*, 17 J. Bus. L. & Ethics 40 (2020).

Restrictions on powers of the Board).[9]

3.8. **Annual General meeting and Extraordinary General Meeting- AGMs & EGMs (Section 96-111):** A company is required to hold an AGM once every calendar year to discuss various matters of general importance such as appointment of directors, financial statements, etc. while the EGMs are called for specific and urgent purposes requiring shareholders' approval.[10]

3.9. **Regulatory Authority and enforcement (Section 211-216):** The Registrar of Companies and Securities and Exchange Board of India (SEBI) are responsible for overseeing compliance with the provisions of the Act.[11]

3.10. **Role of Company Secretary (Section 205):** the Company Secretary plays a crucial role in ensuring that the company adheres to applicable secretarial standards and reports to the board about compliance with the provisions of the Act.

4. Corporate Finance in the context of the Companies Act, 2013

Corporate finance is concerned with the management of the company's funding, capital structure and investment decisions. The Companies Act, 2013 incorporates provisions that regulate corporate finance in India particularly in relation to shares, capital raising and protection of investors[12]. The key provisions highlighting corporate finance under the Act include the following:

4.1. **Capital Structure and Share Capital:** the Act consists of various provisions that regulate the share capital. This includes provisions for kinds of share capital that a company is permitted to issue (**Section 43**), issue and redemption of Preference Shares (**Section 55**), description of process of transfer of shares and specific requirements for public and private companies (**Section 56**).[13]

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[9] A. Dhir, *Corporate Governance and Investor Protection in India: A Critical Analysis of the Companies Act, 2013*, 60 Int'l J. L. & Mgmt. 1162 (2018).
[10] R. Chakraborty, *Shareholder Activism and Minority Protection in India: The Role of the Companies Act, 2013*, 8 Corp. Gov. Rev. 22 (2015).
[11] Securities and Exchange Board of India, Corporate Governance Code for Listed Companies (2014).
[12] V. Sharma, *Corporate Finance Regulations in India: Understanding the Impact of the Companies Act, 2013*, 16 Indian J. Corp. L. 105 (2018).
[13] Indian Inst. of Corp. Affairs, Corporate Governance in India: Legal and Regulatory Overview (2014).

4.2. The Act consists of provisions for **regulating the issue of securities (Section 23).** It defines conditions for making a public offer and the private placement of securities. This involves filing prospectus, obtaining approval from regulators and following prescribed guidelines under the SEBI (Issue of Capital and Disclosure Requirements) Regulations.

4.3. Debentures Issuance is provided for under Section 71 of the Act. It provides for the legal framework for companies to issue debentures and sets out the rights of debenture holders, including redemption. **Section 73 of the Act regulates public deposits** and specifies conditions wherein a company can accept deposits from the public, including the requirement for a rating from a recognized credit rating agency.

4.4. Loans and Borrowings: the Board of Directors cannot borrow money or create charges on company assets beyond a certain limit without prior approval from the shareholders via a special resolution. (**Section 180**). While **Section 186** limits the loans and investments that a company can make in other companies, subject to board's approval and in certain cases, shareholders.[14]

4.5.Financial Reporting and Disclosure: Section 129 of the Act mandates companies to prepare and file financial statements including balance sheet, cash flow statement and profit and loss statement, in accordance with accounting standards prescribed by Ministry of Corporate affairs (MCA).

4.6. Section 123 of the Act outlines process for **declaring and paying dividends** to shareholders and Section 127 of the Act prescribes penalty on companies that fail to pay dividends within the prescribed time and specifies consequences of non-payment.

4.7.Corporate restructuring and Mergers: Section 230-240 govern the restructuring of the companies, including mergers, de-mergers, amalgamations and arrangements. It also mandates the requirement of approval from shareholders, creditors and National Company Law Tribunal (NCLT). [15]

[14] S. Khandelwal, *Corporate Finance: The Role of Debt and Equity in the Companies Act, 2013*, 25 Bus. L.J. 44 (2020)

[15] A.V. Reddy, *Financial Transparency and Accountability in India's Corporates: The Role of Corporate Governance*, 18 Glob. Bus. Rev. 103 (2017).

4.8. Audits and Financial Compliance: Section 139 of the Act mandates appointment of an auditor to review the financial statements and the financial health of the company. They are required to report about any discrepancies or financial mismanagement in the company to the authorities.[16]

5. Impact of the Companies Act, 2013 on Corporate governance and Corporate Finance:

The Introduction of the Act has bought positive changes in both corporate governance and corporate finance practices in India. It has a profound impact on how companies operate, interact with its stakeholders and manage their financial structures. The comprehensive Act has led to improved transparency, boosted investors' confidence and have led to reduced corporate frauds in the country. On one hand, provisions mandating disclosure requirements and financial reporting have led to greater transparency, while on the other hand, provisions regarding directors liabilities and related party transactions help reduce the risk of fraud and mismanagement. Overall this has modernized the regulatory landscape and has contributed to better management practices. [17]

6. Conclusion

Overall, the Companies Act, 2013 has proven to be a significant step forward in strengthening corporate governance and corporate finance in India. By providing a robust legal framework, the Act has laid the foundation for a more accountable and financially sound corporate ecosystem. Despite the challenges in terms of ensuring consistent implementation and enforcement of the Act's provisions across all types of companies, the Act has remained effective in imbibing accountability, transparency and financial stability in India's evolving corporate culture. Future reforms could focus on strengthening enforcement mechanisms, enhancing shareholder activism and addressing the emerging challenges of corporate governance in context of technological advancements and globalised markets.

[16] *id.*
[17] Ministry of Corp. Affairs, Report of the Committee on Corporate Governance Reforms (2022).