



## Mains Practice Question

**Q.** What do you understand by Corporate Governance? Why is it important for the success and sustainability of an organisation? (150 words)

08 Oct, 2020 GS Paper 4 Theoretical Questions

### Approach

- Start by writing a brief introduction about corporate governance.
- Mention the basic components of the Corporate governance
- Discuss the importance of corporate governance for the success and sustainability of an organisation.
- Conclude suitably.

### Introduction

- Corporate governance is defined as a set of systems, processes and principles which ensure that a company is governed in the best interest of all stakeholders. It is about promoting corporate fairness, transparency and accountability.
- Corporate governance plays an important role to protect the rights of thousands of shareholders, who have ownership in the company but do not play an active role in governing day to day business activities. It includes both **social and institutional aspects**.

### Body

#### Corporate governance components:

- **Open to public Information disclosure, high transparency and accountability** are basic important elements of best corporate governance that strives the sustainability of corporations and society.
- To avoid mismanagement, good corporate governance is necessary to enable companies to operate more efficiently, to improve access to capital, mitigate risk and safeguard stakeholders.

#### Importance of corporate governance:

- **Importance of Social Responsibility:** Social responsibility is given a lot of importance in the present time. The corporates have to protect the rights of the customers, employees, shareholders, suppliers, local communities, etc. This is possible only if they use corporate governance.
- **Growing Number of Scams:** In recent years, many scams, frauds and corrupt practices have taken place. Misuse and misappropriation of public money are happening everyday in India and worldwide.
  - It is happening in the stock market, banks, financial institutions, companies and government offices. In order to avoid these scams and financial irregularities, many companies need to adopt corporate governance.
- **Globalization:** Today most big companies are selling their goods in the global market. So, they

have to attract foreign investors and foreign customers. They also have to follow foreign rules and regulations.

- All this requires corporate governance. Without Corporate governance, it is impossible to enter, survive and succeed in the global market.
- **Protect the interest of all stakeholders:** Today, there are many takeovers and mergers in the business world. Corporate governance is required to protect the interest of all the parties during takeovers and mergers.
- The adoption of Corporate governance principles can also play a role in increasing the corporate and business value of companies and help in growth of the national economy.
  - A lack of corporate governance can lead to profit loss, corruption and a tarnished image, not only to the corporation, but to the society, or even worse will influence global as a whole.

### Suggestions to improve corporate governance in India

- Implement the recommendations of **Uday Kotak Panel**, such as:
  - Minimum 6 directors to be on board of listed entities; every listed entity to have at least 1 independent woman director
  - More transparency on appointment of independent directors and should play a more active role on the boards.
- **Diverse boards are better boards:** In this context, 'diverse' is all-encompassing, including gender, ethnicity, skills and experience.
- **Robust risk management policies:** Adoption of effective and robust risk management policies for better decision making as it develops a deeper insight into the risk-reward trade-offs that all Corporations face.
- **Effective governance infrastructure:** Policies and procedures which guide ethical behaviour should form the base of any organizational behaviour. Ensure separation of the line of responsibility between board and management.

### Conclusion

- The primary objective of a corporation is to increase its brand value in the market i.e. society. Successful corporations must operate within the society; to that end, they must maintain the values and norms of the society in which they operate.
- In Indian corporate policies like protecting small shareholders, preventing frauds and malpractices and promoting corporate social responsibility are some of the examples of good corporate governance.