

Corporate Governance
Corporate Governance Voluntary Guidelines
Issued by the MCA, Government of India

“Citizens never support a weak company and birds do not build nests on a tree that does not bear fruits.”

A transparent, ethical and responsible corporate governance framework essentially emanates from the intrinsic will and passion for good governance ingrained in the business entity.

The Ministry of Corporate Affairs has been working towards strengthening of the corporate governance framework through a two pronged strategy. Some aspects which needed to be incorporated in the law have been included in the Companies Bill, 2009 now under examination by Parliament. However, keeping in view the objective of encouraging the use of better practices through voluntary adoption, the Ministry has decided to draft a set of voluntary guidelines which not only serve as a benchmark for the corporate sector but also help them in achieving the highest standard of corporate governance.

1. Board of Directors
 - a. Appointment of Director
 - i. Appointments to the Board
 1. Companies should issue formal letters of appointment to Non-Executive Directors (NEDs) and Independent Director specifying: • The term of the appointment; • The expectation of the Board from the appointed director; the Board-level committee(s) in which the director is expected to serve and its tasks; • The fiduciary duties that come with such an appointment alongwith accompanying liabilities; • Provision for Directors and Officers (D&O) insurance, if any;; • The Code of Business Ethics that the company expects its directors and employees to follow; • The list of actions that a director should not do while functioning as such in the company; and • The remuneration, including sitting fees and stock options etc, if any.
 2. The formal letter should form part of the disclosure to shareholders at the time of the ratification of his/her appointment or re-appointment to the Board. This letter should also be placed by the company on its website, if any, and in case the company is a listed company, also on the website of the stock exchange where the securities of the company are listed.
 - ii. Separation of Offices of Chairman & Chief Executive Officer. The roles and offices of Chairman and CEO should be separated, as far as possible, to promote balance of power.
 - iii. Nomination Committee
 1. The companies may have a Nomination Committee comprising of majority of Independent Directors, including its Chairman. This Committee should consider: • proposals for searching, evaluating, and recommending appropriate Independent Directors and Non-Executive Directors [NEDs], based on an objective and transparent set of guidelines which should be disclosed and should, inter-alia, include the criteria for determining qualifications, positive attributes,

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- independence of a director and availability of time with him or her to devote to the job; • determining processes for evaluating the skill, knowledge, experience and effectiveness of individual directors as well as the Board as a whole.
2. With a view to enable Board to take proper and reasoned decisions, Nomination Committee should ensure that the Board comprises of a balanced combination of Executive Directors and Non-Executive Directors.
 3. The Nomination Committee should also evaluate and recommend the appointment of Executive Directors.
 4. A separate section in the Annual Report should outline the guidelines being followed by the Nomination Committee and the role and work done by it during the year under consideration.
- iv. Number of Companies in which an Individual may become a Director
1. For reckoning the maximum limit of directorships, the following categories of companies should be included:-
 - public limited companies, • private companies that are either holding or subsidiary companies of public companies.
 2. In case an individual is a Managing Director or Whole-time Director in a public company the maximum number of companies in which such an individual can serve as a Non-Executive Director or Independent Director should be restricted to seven.
- b. Independent Directors
- i. Attributes for Independent Directors
 1. The Board should put in place a policy for specifying positive attributes of Independent Directors such as integrity, experience and expertise, foresight, managerial qualities and ability to read and understand financial statements. Disclosure about such policy should be made by the Board in its report to the shareholders. Such a policy may be subject to approval by shareholders.
 2. All Independent Directors should provide a detailed Certificate of Independence at the time of their appointment, and thereafter annually. This certificate should be placed by the company on its website, if any, and in case the company is a listed company, also on the website of the stock exchange where the securities of the company are listed.
 - ii. Tenure for Independent Director
 1. An Individual may not remain as an Independent Director in a company for more than six years.
 2. A period of three years should elapse before such an individual is inducted in the same company in any capacity.

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3. No individual may be allowed to have more than three tenures as Independent Director in the manner suggested in 'i' and 'ii' above.
 4. The maximum number of public companies in which an individual may serve as an Independent Director should be restricted to seven.
- iii. Independent Directors to have the Option and Freedom to meet Company Management periodically
1. In order to enable Independent Directors to perform their functions effectively, they should have the option and freedom to interact with the company management periodically.
 2. Independent Directors should be provided with adequate independent office space and other resources and support by the companies including the power to have access to additional information to enable them to study and analyze various information and data provided by the company management.
- c. Remuneration of Directors
- i. Remuneration
 1. Guiding Principles-Linking Corporate and Individual Performance
 - a. The companies should ensure that the level and composition of remuneration is reasonable and sufficient to attract, retain and motivate directors of the quality required to run the company successfully. It should also be ensured that relationship of remuneration to performance is clear. Incentive schemes should be designed around appropriate performance benchmarks and provide rewards for materially improved company performance. Benchmarks for performance laid down by the company should be disclosed to the members annually.
 - b. Remuneration Policy for the members of the Board and Key Executives should be clearly laid down and disclosed. Remuneration packages should involve a balance between fixed and incentive pay, reflecting short and long term performance objectives appropriate to the company's circumstances and goal.
 - c. The performance-related elements of remuneration should form a significant proportion of the total remuneration package of Executive Directors and should be designed to align their interests with those of shareholders and to give these Directors keen incentives to perform at the highest levels.
 2. Remuneration of Non-Executive Directors (NEDs):
 1. The companies should have the option of giving a fixed contractual remuneration, not linked to profits, to NEDs. The

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- companies should have the option to: (a) Pay a fixed contractual remuneration to its NEDs, subject to an appropriate ceiling depending on the size of the company; or (b) Pay upto an appropriate percent of the net profits of the company.
2. The choice should be uniform for all NEDs, i.e. some should not be paid a commission on profits while others are paid a fixed amount.
 3. If the option chosen is '1(a)' above, then the NEDs should not be eligible for any commission on profits.
 4. If stock options are granted as a form of payment to NEDs, then these should be held by the concerned director until three years of his exit from the Board.
3. Structure of Compensation to NEDs
 - a. The companies may use the following manner in structuring remuneration to NEDs: Fixed component: This should be relatively low, so as to align NEDs to a greater share of variable pay. These should not be more than one-third of the total remuneration package. Variable component: Based on attendance of Board and Committee meetings (at least 75% of all meetings should be an eligibility pre-condition) Additional variable payment(s) for being: the Chairman of the Board, especially if he/she is a nonexecutive chairman the Chairman of the Audit Committee and/or other committees members of Board committees.
 - b. If such a structure (or any similar structure) of remuneration is adopted by the Board, it should be disclosed to the shareholders in the Annual Report of the company.
 4. Remuneration of Independent Directors (IDs)
 - a. In order to attract, retain and motivate Independent Directors of quality to contribute to the company, they should be paid adequate sitting fees which may depend upon the twin criteria of Net Worth and Turnover of companies.
 - b. The IDs may not be allowed to be paid stock options or profit based commissions, so that their independence is not compromised.
- ii. Remuneration Committee
 1. Companies should have Remuneration Committee of the Board. This Committee should comprise of at least

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- three members, majority of whom should be non executive directors with at least one being an Independent Director.
2. This Committee should have responsibility for determining the remuneration for all executive directors and the executive chairman, including any compensation payments, such as retirement benefits or stock options. It should be ensured that no director is involved in deciding his or her own remuneration.
 3. This Committee should also determine principles, criteria and the basis of remuneration policy of the company which should be disclosed to shareholders and their comments, if any, considered suitably. Whenever, there is any deviation from such policy, the justification/reasons should also be indicated/disclosed adequately.
 4. This Committee should also recommend and monitor the level and structure of pay for senior management, i.e. one level below the Board.
 5. This Committee should make available its terms of reference, its role, the authority delegated to it by the Board, and what it has done for the year under review to the shareholders in the Annual Report.
- d. Training of Directors
- i. The companies should ensure that directors are inducted through a suitable familiarization process covering, inter-alia, their roles, responsibilities and liabilities. Efforts should be made to ensure that every director has the ability to understand basic financial statements and information and related documents/papers. There should be a statement to this effect by the Board in the Annual Report.
 - ii. Besides this, the Board should also adopt suitable methods to enrich the skills of directors from time to time.
- e. Enabling Quality Decision making The Board should ensure that there are systems, procedures and resources available to ensure that every Director is supplied, in a timely manner, with precise and concise information in a form and of a quality appropriate to effectively enable/ discharge his duties. The Directors should be given substantial time to study the data and contribute effectively to Board discussions.
2. Risk Management
- a. The Board, its Audit Committee and its executive management should collectively identify the risks impacting the company's business and document their process of risk identification, risk minimization, risk optimization as a part of a risk management policy or strategy.
 - b. The Board should also affirm and disclose in its report to members that it has put in place critical risk management framework across the company, which is overseen once every six months by the Board. The disclosure should also include a statement of those elements of risk, that the Board feels, may threaten the existence of the company.
3. Evaluation of Performance of Board of Directors, Committees thereof and of Individual Directors. The Board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors. The Board should state in the Annual Report how

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performance evaluation of the Board, its committees and its individual directors has been conducted.

4. Board to place Systems to ensure Compliance with Laws
 - a. In order to safeguard shareholders' investment and the company's assets, the Board should, at least annually, conduct a review of the effectiveness of the company's system of internal controls and should report to shareholders that they have done so. The review should cover all material controls, including financial, operational and compliance controls and risk management systems.
 - b. The Directors' Responsibility Statement should also include a statement that proper systems are in place to ensure compliance of all laws applicable to the company. It should follow the "comply or explain" principle.
 - c. For every agenda item at the Board meeting, there should be attached an "Impact Analysis on Minority Shareholders" proactively stating if the agenda item has any impact on the rights of minority shareholders. The Independent Directors should discuss such Impact Analysis and offer their comments which should be suitably recorded.
5. Audit Committee – Constitution, the companies should have at least a three-member Audit Committee, with Independent Directors constituting the majority. The Chairman of such Committee should be an Independent Director. All the members of audit committee should have knowledge of financial management, audit or accounts.
6. Audit Committee – Enabling Powers:
 - a. The Audit Committee should have the power to - • have independent back office support and other resources from the company; • have access to information contained in the records of the company; and • obtain professional advice from external sources.
 - b. The Audit Committee should also have the facility of separate discussions with both internal and external auditors as well as the management.
7. Audit Committee - Role and Responsibilities
 - a. The Audit Committee should have the responsibility to - • monitor the integrity of the financial statements of the company; • review the company's internal financial controls, internal audit function and risk management systems; • make recommendations in relation to the appointment, reappointment and removal of the external auditor and to approve the remuneration and terms of engagement of the external auditor; • review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process.
 - b. The Audit Committee should also monitor and approve all Related Party Transactions including any modification/amendment in any such transaction.
 - c. A statement in a prescribed/structured format giving details about all related party transactions taken place in a particular year should be included in the Board's report for that year for disclosure to various stake holders.
8. Appointment of Auditors
 - a. The Audit Committee of the Board should be the first point of reference regarding the appointment of auditors.
 - b. The Audit Committee should have regard to the profile of the audit firm, qualifications and experience of audit partners, strengths and weaknesses, if any, of the audit firm and other related aspects.

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- c. To discharge its duty, the Audit Committee should:
 - discuss the annual work programme and the depth and detailing of the audit plan to be undertaken by the auditor, with the auditor;
 - examine and review the documentation and the certificate for proof of independence of the audit firm, and
 - recommend to the Board, with reasons, either the appointment/re-appointment or removal of the statutory auditor, along with the annual audit remuneration.
- d. Certificate of Independence
 - i. Every company should obtain a certificate from the auditor certifying his/its independence and arm's length relationship with the client company.
 - ii. The Certificate of Independence should certify that the auditor together with its consulting and specialized services affiliates, subsidiaries and associated companies or network or group entities has not/have not undertaken any prohibited non-audit assignments for the company and are independent vis-à-vis the client company.
- e. Rotation of Audit Partners and Firms
 - i. In order to maintain independence of auditors with a view to look at an issue (financial or non-financial) from a different perspective and to carry out the audit exercise with a fresh outlook, the company may adopt a policy of rotation of auditors which may be as under:-
 - Audit partner - to be rotated once every three years
 - Audit firm - to be rotated once every five years.
 - ii. A cooling off period of three years should elapse before a partner can resume the same audit assignment. This period should be five years for the firm.
- 9. Need for clarity on information to be sought by auditor and/or provided by the company to him/it
 - a. With a view to ensure proper and accountable audit, there should be clarity between company management and auditors on the nature and amount of information/documents/ records etc and periodicity/frequency for supply/obtaining such information/documents/ records etc.
 - b. In any case the auditor concerned should be under an obligation to certify whether he had obtained all the information he sought from the company or not. In the latter case, he should specifically indicate the effect of such non receipt of information on the financial statements.
- 10. Appointment of Internal Auditor, In order to ensure the independence and credibility of the internal audit process, the Board may appoint an internal auditor and such auditor, where appointed, should not be an employee of the company.
- 11. Institution of Mechanism for Whistle Blowing, Since the Board has the overarching responsibility of ensuring transparent, ethical and responsible governance of the company, it is important that the Board processes and compliance mechanisms of the company are robust. To ensure this, the companies may get the Secretarial Audit conducted by a competent professional. The Board should give its comments on the Secretarial Audit in its report to the shareholders.
 - a. The companies should ensure the institution of a mechanism for employees to report concerns about unethical behaviour, actual or

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suspected fraud, or violation of the company's code of conduct or ethics policy.

- b. The companies should also provide for adequate safeguards against victimization of employees who avail of the mechanism, and also allow direct access to the Chairperson of the Audit Committee in exceptional cases.