CORPORATE GOVERNANCE IN INDIA: LESSONS FROM RECENT SCAMS

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ABSTRACT

Corporate governance in India has evolved considerably over the past three decades, shaped in no small measure by a series of high-profile corporate frauds that exposed the fragility of existing regulatory mechanisms. This article undertakes a critical examination of the systemic failures in corporate governance that facilitated some of India's most consequential scams, with particular emphasis on the Satyam Computer Services fraud of 2009, the Punjab National Bank–Nirav Modi scam of 2018, and the IL&FS liquidity crisis of 2018. Through an analysis of the relevant legal provisions under the Companies Act, 2013, the Securities and Exchange Board of India Act, 1992, and allied regulatory frameworks, the article identifies recurring patterns of board dysfunction, audit inadequacy, and regulatory arbitrage that enabled these frauds to persist undetected. The article concludes by evaluating the reforms that have followed in the wake of these events and by offering observations on the gaps that continue to undermine effective corporate governance in India.

Keywords: Corporate Governance, Companies Act 2013, SEBI, Satyam, PNB Fraud, IL&FS, Independent Directors, Audit Committee, Whistleblower Protection, Board Accountability.

INTRODUCTION

In contemporary commercial law, the idea of corporate governance is crucial. In its most basic form, it refers to the set of guidelines, procedures, and practices that govern how a business is run. It provides the framework for balancing and enforcing the rights and obligations of various stakeholders, including shareholders, directors, management, regulators, and creditors. Sound corporate governance is essential in a market economy like India's, not just to safeguard

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investor interests but also to maintain macroeconomic stability and public trust in the financial system.

In comparison, India's involvement in the corporate governance debate is very new. Only in the 1990s, with the start of economic liberalisation in 1991, did the nation's regulatory framework in this area start to take shape. Established under the Securities and Exchange Board of India Act, 1992,[1] the Securities and Exchange Board of India (henceforth referred to as "SEBI") became the primary regulator of listed companies, while the Companies Act underwent a series of revisions that culminated in the comprehensive re-enactment[2] of 2013[3]. The first comprehensive attempt to institutionalise governance standards for publicly traded companies was the addition of Clause 49 to the Listing Agreement, which was strengthened by the Narayana Murthy Committee in 2003[4] and followed the recommendations of the Kumar Mangalam Birla Committee in 1999[5].

Despite these advancements, India has had a number of significant corporate governance failures. These incidents have sparked crises of confidence in the integrity of India's corporate sector in addition to causing financial losses for creditors and shareholders. In hindsight, every crisis has been a diagnostic experiment that has exposed systemic flaws in the institutional and legal structure that controls corporate behaviour.

The flow of this article is as follows. Corporate governance is placed in its theoretical and normative framework in Part II. As case studies of governance failure, Part III looks at three major scams: Satyam Computer Services, the Punjab National Bank–Nirav Modi fraud, and the IL&FS disaster. The legislative and regulatory reactions that these events prompted are examined in Part IV. Part V identifies the persistent deficiencies in India's governance regime and offers recommendations for reform. Part VI concludes.

[1] Securities and Exchange Board of India Act 1992.
[2]Ministry of Corporate Affairs, *Report of the Expert Committee on Company Law* (2005) ('JJ Irani Committee Report').
[3] Companies Act 2013, s 134,149,177.
[4] SEBI, *Report of the Narayana Murthy Committee* (2003) para 2.1.
[5] Ministry of Corporate Affairs, *Report of the Kumar Mangalam Birla Committee* (1999) 12–15.

CORPORATE GOVERNANCE: THEORETICAL FOUNDATIONS AND THE INDIAN FRAMEWORK

Two theoretical paradigms are the main forces behind the scholarly literature on corporate governance. The first is the agency theory, which views the company as a hub of agreements between agents (directors and managers) and principals (shareholders). The conflicting interests of these two groups give birth to the agency problem:[6][7] directors may behave in ways that are detrimental to the welfare of shareholders, pursue personal profit, or solidify their positions. Under this concept, corporate governance mechanisms—such as independent boards, audit committees, executive compensation plans, and disclosure standards—are intended to restrain managerial behaviour and bring it into line with the interests of shareholders.

The second paradigm, known as the stakeholder theory, has a more expansive stance, arguing that businesses have responsibilities to communities, workers, creditors, consumers, shareholders, and society at large[8]. This viewpoint has been increasingly incorporated into Indian corporate law; the Companies Act of 2013 establishes mandatory Corporate Social Responsibility (CSR) obligations, and SEBI's Listing Obligations and Disclosure Requirements (LODR) Regulations of 2015[9] mandate that listed companies use Business Responsibility Reports to report on their performance in relation to environmental, social, and governance (ESG) parameters.

A tripartite structure is the foundation of the Indian corporate governance framework. The Companies Act, 2013, which specifies the composition and responsibilities of boards of directors and regulates the incorporation, management, and winding up of companies, is administered by the Ministry of Corporate Affairs (MCA). By requiring improved board composition, audit committee operations, and ongoing transparency, SEBI enhances these criteria for listed businesses under the LODR Regulations, 2015. The Banking Regulation Act of 1949 grants the Reserve Bank of India (RBI)[10] regulatory authority over financial

[6] Adolf A Berle and Gardiner C Means, The Modern Corporation and Private Property (Transaction Publishers 1991).
[7] Michael C Jensen and William H Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 *Journal of Financial Economics* 305.
[8] R Edward Freeman, *Strategic Management: A Stakeholder Approach* (Pitman 1984).
[9] SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015, reg 17.
[10] Reserve Bank of India Act 1934.

institutions. Despite its extensive coverage, this multi-regulator strategy has historically led to coordination breakdowns that astute corporate players have taken advantage of.

CORPORATE GOVERNANCE FAILURES: A CASE STUDY ANALYSIS

The 2009 Satyam Computer Services Scam:[11] In the history of independent India, the Satyam scandal continues to be the most significant corporate fraud. The chairman and founder of Satyam Computer Services Limited[12], which at the time was the fourth-largest information technology business in India, Ramalinga Raju, publicly admitted on January 7, 2009, that he had been systematically falsifying the company's finances for almost seven years. According to the confession, the company's September 2008 balance sheet showed an inflated debtors' position of Rs. 490 crores, an understated liability of Rs. 1,230 crores due to funds arranged by Raju personally, a fictitious cash and bank balance of about Rs. 5,040 crores, and accrued interest of Rs. 376 crores that did not exist.

Satyam is a prime example of corporate governance failure, not only because of the size of the fraud but also because of the remarkable systemic flaws that allowed it to continue for so long. It is clear that the board of directors, which comprised a number of eminent independent directors with outstanding professional backgrounds, did not exercise effective oversight. The board had authorised the purchase of two infrastructure firms supported by the Raju family at a combined valuation of Rs. 1,600 crores, a deal that would have redirected corporate cash to related parties, just minutes before the scam came to light, without conducting sufficient due diligence.

Price Waterhouse[13], Price Waterhouse Coopers' Indian affiliate, served as the statutory auditor, and its participation was closely examined. The auditors allegedly accepted confirmations from bank branches without independently confirming the cash balances shown in the accounts. This represented a significant divergence from the auditing criteria that would typically identify this kind of variation. Following this, SEBI issued debarment orders after finding the auditors guilty of professional misconduct. The Satyam scam revealed a number of systemic flaws. First, the audit committee's structure and operations were inefficient; it had simply held ceremonial meetings and had not thoroughly examined significant transactions as required by the seriousness of its role. Second, despite the formal existence of independent directors, the

[11] Serious Fraud Investigation Office, *Satyam Scam Investigation Report* (2009).
[12] Satyam Computer Services Ltd, Chairman's Letter (7 January 2009).
[13] *SEBI v Price Waterhouse* (2018) SEBI Order WTM/GM/EFD/1/2018.

promoter's capacity to tightly control information flows within the company demonstrated the board's actual lack of independence. Third, internal dissenters, if any, had no safe way to voice their concerns because there was no strong whistleblower system in place.

The legislative reaction was noteworthy. In direct response to Satyam, the Companies Act of 2013 significantly tightened the rules governing audit committees, requiring them to be made up of a majority of independent directors, have adequate financial literacy, and have the authority to independently look into financial irregularities. Later, the ineffective self-regulatory model was replaced by the National Financial Reporting Authority (NFRA), an independent supervision agency for the auditing profession.

The 2018 Punjab National Bank-Nirav Modi Scam:[14] One of the biggest public sector banks in India, Punjab National Bank (PNB), informed stock exchanges in February 2018 that it had found fraudulent transactions totalling over Rs. 11,400 crores, which was later increased to about Rs. 13,500 crores. The fraud, which involved the issuance of fictitious Letters of Undertaking (LoUs), which are similar to bank guarantees used to secure buyers' credit from foreign branches of other Indian banks, was planned over a period of almost seven years by diamantaire Nirav Modi and his associates in collusion with some officials of PNB's Brady House branch in Mumbai.

The fraud's workings were educational. By taking advantage of the fact that PNB's central banking system (CBS) was not connected to the SWIFT interbank messaging technology, the implicated bank officials issued LoUs on behalf of Nirav Modi's businesses without documenting them in the system. Because of this technology flaw, fake LoUs might be sent to foreign correspondent banks without creating an internal audit trail in PNB's own systems. When PNB eventually rejected the unapproved promises, the beneficiary banks that had honoured these LoUs in good faith were left with significant risk.

From a corporate governance perspective, the PNB fraud illustrates a distinct but equally serious set of failures. Public sector banks in India, by virtue of the government's majority shareholding and the concomitant political influence over key appointments, operate under governance conditions that differ materially from those of privately owned corporations. The board of directors, which is supposed to have fiduciary responsibility for the bank's operations, didn't really monitor operational risk management. Internal audit functions, which should have

[14] Central Bureau of Investigation, *PNB Fraud Case Report* (2018).

detected the divergence between CBS records and SWIFT transactions, failed to do so for nearly seven years, pointing to systemic deficiencies in risk culture and audit rigour.

The Enforcement Directorate initiated proceedings under the Prevention of Money Laundering Act 2002[15], while the Central Bureau of Investigation registered criminal cases against the accused. The RBI subsequently issued directives mandating the integration of SWIFT with CBS across all scheduled commercial banks. The incident strengthened calls for depoliticising appointments to public sector bank boards and for increased board-level expertise in technology risk management at the level of governance reform.

The 2018 IL&FS Liquidity Crisis: With a vast network of more than 300 subsidiaries and affiliates involved in financial services, road construction, and infrastructure finance, Infrastructure Leasing & Financial Services Limited (IL&FS) was a systemically significant non-banking financial company (NBFC). A liquidity crisis in India's NBFC and mutual fund industries was caused by IL&FS's September 2018[16] default on several loan obligations, which also sent shockwaves through the country's larger financial markets. The group owed about Rs. 94,000 crores in total debt at the time of its demise.

A particularly complicated governance story is presented by the IL&FS debacle. The group's board comprised distinguished professionals and was occasionally presided over by seasoned administrators; however, the board was largely unaware of or insufficiently involved with the group's increasing leverage and declining asset quality. Critics have pointed to the opacity of the group's inter-company transactions, which were structured in a manner that effectively concealed the true extent of financial stress at the group level from minority shareholders, creditors, and regulators alike.

Up until just before the default, the credit rating agencies that rated IL&FS's debt instruments kept giving its securities investment-grade ratings, which raised serious concerns about the quality of their due diligence and the conflicts of interest present in the issuer-pays model of credit rating. The statutory auditors were also under investigation because they approved financial statements that, in retrospect, did not accurately depict the group's financial situation. The Government of India was permitted by the National Company Law Tribunal (NCLT)[17] in

[15] Prevention of Money Laundering Act 2002.
[16] Infrastructure Leasing & Financial Services Ltd Crisis Report (Ministry of Corporate Affairs 2018).
[17] National Company Law Tribunal, *Union of India v IL&FS Ltd* (2018) Order dated 1 October 2018.

October 2018 to replace the current IL&FS board and establish a new board to oversee the resolution process.

The systemic hazards associated with big, linked financial conglomerates operating beyond the boundaries of direct banking regulation were also brought to light by the IL&FS incident. The emerging insolvency framework was put to the test in the context of a complex group with a heterogeneous asset base and diverse creditor classes when the Insolvency and Bankruptcy Code, 2016[18], was subsequently invoked for the resolution of some IL&FS entities. This was a challenge for which the Code's architecture was not fully prepared.

REGULATORY AND LEGISLATIVE REACTIONS

Indian corporate governance law has significantly changed as a result of the legislative and regulatory reactions sparked by the scams covered in Part III. Enacted in the immediate wake of Satyam, the Companies Act, 2013, introduced several revolutionary rules.

For the first time, listed firms were required by the Act to designate at least one-third of their board as independent directors. Independent directors are appointed for a set term of five years, renewed once with shareholder approval by a special resolution. They must meet a dual negative test, which requires them to have no meaningful financial tie with the firm and no link with its management. The purpose of these regulations was to prevent directors who ostensibly served as watchdogs from being subservient to the promoter group. The SEBI (LODR) (Amendment) Regulations, 2018, significantly adopted the recommendations made by the Uday Kotak Committee[19] on Corporate Governance, which was established by SEBI in 2017 and advocated raising the minimum number of independent directors on the boards of listed companies. During the post-Satyam era.

The whistleblower framework attracted a lot of attention. Every listed business and other specified classes of corporations are now required by Section 177 of the Corporations Act, 2013, to set up a monitoring system for directors and workers to report legitimate concerns. Similar requirements are found in SEBI's LODR Regulations, which mandate that listed companies have a functioning whistleblower policy with sufficient protections against complainant abuse. However, academics have pointed out that the protection of private sector whistleblowers is dependent on company-specific policies of varying quality due to the lack of

[18] Insolvency and Bankruptcy Code 2016.
[19] Report of the Uday Kotak Committee on Corporate Governance (SEBI 2017).

a comprehensive whistleblower protection law that applies to the private sector, similar to the Public Interest Disclosure (Protection of Informers) Act, which has not yet been operationalised in a comprehensive form.

A major structural change of audit oversight occurred with the creation of the National Financial Reporting Authority (NFRA) under Section 132 of the Companies Act, 2013. NFRA has the authority to establish and uphold accounting and auditing standards, look into allegations of professional misconduct by auditors of designated kinds of businesses, and apply penalties, including debarment. This replaces the previous system in which audit quality was overseen by the Institute of Chartered Accountants of India (ICAI), a body made up of and controlled by the very profession it regulates. This system was considered insufficient due to the inherent conflicts of interest.

The IL&FS crisis forced the RBI to strengthen its supervision of big NBFCs at the level of systemic risk regulation, enacting scale-based regulation that subjected "upper layer" NBFCs to bank-like prudential standards, such as required listing and improved board governance. While SEBI has increased its ability to enforce laws pertaining to unfair and fraudulent trading practices in securities markets, the Competition Commission of India has also stepped up its examination of transactions involving systemically large organisations.

PERSISTENT DEFICIENCIES AND THE ROAD AHEAD

The efficacy of India's corporate governance framework is nevertheless compromised by a number of structural flaws, despite the legal advancements mentioned above. If reform is to be intentional rather than merely reactive, an honest assessment of these gaps is required.

The first and possibly most important shortcoming has to do with independent directors' actual independence. Formal independence is required by law, but substantive independence is compromised by the appointment process, where the promotional group has significant influence. The nomination process for board members should be transparent and free from undue influence from the company's controlling shareholders, according to the OECD Principles of Corporate Governance[20]. To consistently operationalise this notion, India has not yet established institutionalised systems, such as independent nominating committees with true autonomy.

[20] OECD, *G20/OECD Principles of Corporate Governance* (OECD Publishing 2015).

The control of public sector businesses, such as banks, is a second issue. An inherent tension arises from the government's dual role as the largest shareholder and the sovereign regulator. Political factors still have an impact on appointments to the boards of public sector banks and financial institutions, and the short terms of chief executives who are often replaced before they can make significant changes affect organisational accountability and strategic continuity. Regulatory arbitrage between the MCA's corporate governance system and the RBI's banking regulatory regime can result in hazardous governance vacuums, as the PNB fraud showed.

Third, when audit committees are composed of directors who lack the institutional bravery or financial ability to question management, the effectiveness of audit committees as a governance instrument is still questionable. The law can't require real engagement, but it can specify requirements. The concentration of audit market share among a few major audit firms is a related issue that raises systemic risk in the event that any of them have an integrity or capacity crisis.

Fourth, a sophisticated and analytically capable investor community is necessary for India's disclosure-based regulatory philosophy, which is based on the strategy suggested by SEBI's numerous committees and in line with global best practices. In a market where retail investors comprise a significant proportion of participants and where financial literacy remains uneven, the disclosure of complex financial information does not always translate into effective market discipline.

Fifth, enforcement is still consistently insufficient. Even though SEBI's enforcement efforts have become more vigorous in recent years, the Securities Appellate Tribunal, higher courts, and SEBI's own adjudicating officers continue to adjudicate cases slowly. The clarity and promptness of regulatory fines are crucial for their deterrent effect; lengthy proceedings weaken both.

Lastly, there are still issues with related-party transaction legislation, which is at the core of several governance failures, including Satyam. Although shareholder approval is required for significant related-party transactions under the Companies Act, 2013, and the LODR Regulations, the definitional thresholds and disclosure requirements have undergone numerous revisions, reflecting the challenge of finding a balance between investor protection and operational flexibility for legitimate business transactions.

CONCLUSION

Reactive legislation has played a major role in India's corporate governance reform trajectory. The lessons learned from Satyam influenced the Companies Act of 2013; the PNB fraud sped up the tightening of banking regulations; and the IL&FS scandal increased the regulation of huge NBFCs. Although crisis-driven reform is preferable to no reform at all, it has a drawback in that it only fixes the flaws that a single fraud has revealed, leaving the latent vulnerabilities intact.

The development of an attitude of accountability that is independent of the fear of punishment is necessary for a more long-lasting approach to corporate governance in boardrooms, audit firms, credit rating agencies, and regulatory organisations. This calls for a change in governance culture from one that is compliance-based to one that is principles-based, where directors and auditors internalise their responsibilities as stewards of financial trust rather than just as fulfillers of legal tasks.

At the institutional level, India would gain from a more cohesive corporate governance regulatory framework that lessens the coordination gaps that have historically been exploited by clever actors. In an era of digitalised financial infrastructure, it is now unavoidable to incorporate technology risk governance into board-level mandates, especially for financial institutions. Protecting senior bank executives and independent directors from political interference during the appointment process is equally crucial.

In a deeper sense, the scams discussed in this article have been educational because they have shown that governance failure is rarely the result of a single mistake or a single delinquent individual. Instead, it is the result of a system where several safeguards' boards, auditors, rating agencies, and regulators fail at the same time, sometimes with the hope that another will step in. The real challenge of reform is to address this systemic aspect of governance failure.