INTRODUCTION TO CORPORATE GOVERNANCE IN INDIA: FOUNDATIONS, EVOLUTION, AND RELEVANCE

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Corporate governance is no longer understood merely as a compliance obligation imposed by company law or securities regulation. In contemporary corporate practice, it represents a foundational business infrastructure, a framework through which decision-making authority is allocated, accountability is enforced, and long-term value is preserved. At its core, corporate governance addresses a fundamental problem inherent in corporate structures: the separation of ownership, control, and management, and the resulting need for oversight, discipline, and transparency.

Global thought leadership has consistently articulated corporate governance as a system rather than a rulebook. The OECD Principles of Corporate Governance define it as the set of relationships between a company's management, its board, its shareholders, and other stakeholders, providing the structure through which corporate objectives are set and performance is monitored. This understanding has increasingly influenced domestic legal frameworks, including in India, where governance norms are no longer confined to listed companies but are embedded into the statutory duties of directors and key managerial personnel under the Companies Act, 2013.[1]

For founders and promoters of unlisted and closely-held companies, corporate governance is often perceived as an external imposition something triggered by regulatory scrutiny, institutional investment, or public listing. This perception is both incomplete and commercially risky. In practice, governance functions as internal business infrastructure, comparable to financial controls, intellectual property ownership, or capital structuring. Weak governance structures tend to surface not as abstract compliance failures, but as operational friction—unclear authority, conflicted decision-making, inadequate disclosures, and disputes between founders, management, and investors.

From an investor perspective, governance is rarely evaluated in isolation. Institutional investors, private equity funds, and strategic acquirers increasingly treat governance quality as a threshold diligence issue, influencing valuation, risk allocation, and exit feasibility.[2] Governance failures are often early indicators of deeper structural risks, including poor capital discipline, excessive promoter control, and weak internal controls. Conversely, early adoption of governance frameworks enables companies to scale responsibly, absorb external capital with minimal disruption, and transition smoothly across growth stages.

Indian corporate governance has evolved in response to both domestic corporate failures and global best practices. Legislative reforms, judicial interpretation, and policy interventions have progressively shifted governance from a voluntary "best practice" model

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[1] Companies Act, 2013, ss. 166, 173, 177, 178
[2] OECD (2023), G20/OECD Principles of Corporate Governance 2023, OECD Publishing, Paris, https://doi.org/10.1787/ed750b30-en

to a mandatory legal and fiduciary framework.[3] Importantly, this evolution signals that governance is not intended to constrain entrepreneurship, but to institutionalise trust—between founders and investors, boards and management, and companies and the markets they operate in.

This article sets the foundation for the Corporate Governance series by examining the conceptual underpinnings, evolution, and legal architecture of corporate governance in India, with particular emphasis on its relevance to founders, promoters, and investors in unlisted companies.

What Is Corporate Governance? Meaning, Scope, and Purpose

Corporate governance refers to the framework through which companies are directed, controlled, and held accountable. It is not a singular statute or a fixed set of rules, but a system of relationships, processes, and institutional checks that regulate how corporate power is exercised and how corporate objectives are pursued. At its essence, corporate governance addresses the manner in which decision-making authority is structured within a company and the mechanisms through which such authority is monitored and restrained.

Internationally, corporate governance has been articulated as a relational framework rather than a compliance construct. The OECD Principles of Corporate Governance describe it as the network of relationships between a company's management, its board of directors, its shareholders, and other stakeholders, providing the structure through which corporate objectives are set, performance is monitored, and accountability is ensured. Indian corporate law reflects a similar understanding, particularly through the codification of directors' fiduciary duties and board responsibilities under the Companies Act, 2013, which embeds governance principles directly into statutory obligations rather than treating them as optional best practices.[4]

The scope of corporate governance extends across multiple layers of a corporate entity. Internally, it governs the role and responsibilities of the board of directors, the conduct of management and key managerial personnel, and the rights and protections available to shareholders, including minority shareholders. Externally, it intersects with the interests of creditors, regulators, and investors, particularly in relation to disclosure standards, financial discipline, and risk oversight. Governance typically covers matters such as board composition and functioning, internal controls and audit mechanisms, transparency and disclosures, conflict management, and ethical conduct. It does not, however, seek to regulate day-to-day commercial operations or substitute managerial discretion with regulatory oversight.

A central theoretical foundation of corporate governance lies in the separation of ownership, control, and management. In corporate structures, shareholders provide capital, boards

[3] SEBI, Report of the Kumar Mangalam Birla Committee on Corporate Governance (1999) https://www.sebi.gov.in/sebi_data/commondocs/corpgov1_p.pdf; SEBI, Report of the Kotak Committee on Corporate Governance (2017) https://www.sebi.gov.in/sebi_data/attachdocs/oct-2017/1509102194616.pdf
[4] Companies Act, 2013, ss. 166, 173–178

exercise oversight, and management conducts operations. This separation gives rise to agency risks, information asymmetry, and potential conflicts of interest. Corporate governance operates as a corrective framework to mitigate these risks by imposing fiduciary duties, disclosure obligations, and accountability standards on those entrusted with control. These concerns are not limited to widely held public companies; they are equally relevant in founder-driven and closely held companies, where concentration of control can amplify governance risks.

The purpose of corporate governance is therefore threefold. Legally, it enforces fiduciary discipline and provides remedies against mismanagement, oppression, and abuse of power. Commercially, it enhances investor confidence, improves capital efficiency, and supports long-term value creation. Institutionally, it contributes to market integrity and trust in corporate forms. For unlisted and emerging companies, governance assumes an additional dimension—it operates as a structural and contractual framework, shaping board rights, shareholder arrangements, and information flows well before statutory thresholds or public scrutiny apply. Early governance choices often have lasting consequences, influencing fundraising outcomes, control dynamics, and exit readiness.

The Need for Corporate Governance

1. Corporate Governance as a Response to Structural Corporate Risks

Corporate governance arises from the inherent structural features of the corporate form. Companies are characterised by a separation between ownership, control, and management, which creates agency risks, information asymmetry, and potential conflicts of interest. Indian corporate law recognises these structural vulnerabilities by imposing fiduciary duties on directors and key managerial personnel under the Companies Act, 2013, thereby embedding governance obligations into the legal architecture of companies rather than treating them as optional best practices.[5]

These risks are not confined to widely held public companies. In closely held and founder-driven companies, concentration of control, informal decision-making, and weak documentation can amplify governance failures, often surfacing during fundraising, disputes, or exit transactions.

2. Protection of Shareholders and Minority Interests

A core need for corporate governance lies in the protection of shareholder interests, particularly minority shareholders. Indian jurisprudence has consistently recognised that unchecked majority or promoter control can result in oppression, mismanagement, and abuse of corporate power. Statutory remedies under the Companies Act, 2013 expressly address such conduct, reflecting the legislature's intent to use governance mechanisms as corrective tools against inequitable conduct.[6]

[5] Companies Act, 2013, s. 166
[6] Companies Act, 2013, ss. 241–242

Judicial decisions have further reinforced that corporate governance is integral to ensuring fairness, transparency, and equitable treatment of shareholders, especially in unlisted companies where market discipline and disclosure norms are limited.[7]

3. Accountability of Boards, Promoters, and Management

Corporate governance operates as a framework for accountability. Directors and officers are entrusted with corporate assets and decision-making authority and are therefore subject to fiduciary duties of care, loyalty, and good faith. Governance mechanisms ensure that such duties are not merely theoretical but enforceable.

4. Investor Confidence and Capital Formation

From an investment perspective, governance quality is a threshold consideration. Institutional investors and private equity funds increasingly align their expectations with international benchmarks such as the OECD Principles of Corporate Governance (1999; revised 2015 and in 2023) and governance frameworks developed by the International Finance Corporation (2009). Weak governance structures often translate into valuation discounts, heightened risk allocation, and delayed exits.

5. Risk Management and Corporate Longevity

Governance failures frequently precede financial distress, regulatory intervention, and reputational harm. Indian policy discourse, particularly through expert committee reports, has recognised corporate governance as a preventive mechanism essential for long-term sustainability and market integrity.

Core Pillars of Corporate Governance

Corporate governance is not a collection of isolated rules but a principle-based framework anchored in certain foundational pillars. These pillars operate collectively to regulate the exercise of corporate power, ensure accountability, and preserve stakeholder confidence.

1. Accountability

Accountability lies at the heart of corporate governance. It requires that those who exercise decision-making authority—typically the board of directors and senior management—are answerable for their actions and decisions. Accountability ensures that corporate power is exercised within defined mandates and that decision-makers remain subject to oversight and consequence. Globally, governance frameworks emphasise the board's accountability to the company and its shareholders, particularly in relation to strategy, risk oversight, and stewardship of corporate assets.[8]

[7] *Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.*, (1981) 3 SCC 333.
[8] OECD (2023), G20/OECD Principles of Corporate Governance 2023, OECD Publishing, Paris, https://doi.org/10.1787/ed750b30-en.

2. Transparency

Transparency refers to the timely, accurate, and reliable disclosure of material information relating to a company's operations, financial position, governance structures, and risks. It functions as a critical control mechanism by reducing information asymmetry between insiders and external stakeholders. International governance standards consistently recognise transparency as essential for informed shareholder decision-making, market discipline, and investor confidence, irrespective of whether a company is publicly listed or privately held.[9]

3. Fairness

Fairness requires equitable treatment of all shareholders and stakeholders and seeks to prevent abuse arising from concentrated control or informational advantages. This pillar underpins protections against self-dealing, conflicts of interest, and discriminatory conduct. Globally accepted governance principles emphasise that minority shareholders should be protected against unfair actions by controlling shareholders or management, as fairness is integral to trust in corporate structures and capital markets.

4. Responsibility and Ethical Conduct

Responsibility extends beyond compliance with law to encompass ethical conduct, prudent risk management, and long-term sustainability. Governance frameworks increasingly recognise that boards must act as responsible stewards of the enterprise, balancing short-term performance with long-term value creation. Ethical governance and responsible decision-making are now regarded as essential components of corporate resilience and legitimacy.

These pillars are interdependent and mutually reinforcing. A failure in any one pillar often weakens the entire governance framework, underscoring the need for a holistic and principle-based approach to corporate governance.

Evolution of Corporate Governance in India: A Chronological Perspective

1. Pre-Liberalisation Era (Pre-1991): Promoter Control and Limited Governance

Prior to economic liberalisation, Indian corporate structures were predominantly promoter-driven, closely held, and insulated from market scrutiny. Corporate governance was largely understood as compliance with the Companies Act, 1956, with limited emphasis on board independence, disclosures, or minority shareholder protection. Capital markets were shallow, institutional investors were limited, and disclosure and board independence norms were minimal. Governance concerns typically arose only ex post, through judicial remedies addressing oppression, mismanagement, or breach of fiduciary duties.

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[9] World Bank, *Corporate Governance: A Framework for Implementation* (2000) https://documents1.worldbank.org/curated/en/831651468781818619/pdf/30446.pdf

A notable early inflection came from industry itself. The **Confederation of Indian Industry** issued the *Code of Desirable Corporate Governance* in 1998, marking the first structured attempt to articulate governance standards in India. Though voluntary, the CII Code emphasised board responsibility, transparency, and accountability, and acknowledged that governance quality directly affected investor confidence and access to capital.

2. SEBI-Led Institutionalisation: Birla Committee (1999–2001)

The formal institutionalisation of corporate governance began with the Kumar Mangalam Birla Committee (1999), constituted by the Securities and Exchange Board of India. The Committee's recommendations included norms relating to board composition, audit committees, independent directors, and enhanced disclosures.[10]

This phase marked a decisive shift from voluntary best practices to enforceable regulatory standards, positioning governance as a central component of market integrity.

3. Strengthening Audit Integrity and Financial Governance (2002)

Governance reforms were further deepened through the Naresh Chandra Committee (2002), which focused on audit governance, auditor independence, and financial disclosures. The Committee highlighted the role of accurate financial reporting and independent auditing as essential pillars of governance, particularly in restoring investor trust after global accounting scandals. Its recommendations reinforced the linkage between governance, financial transparency, and accountability.[11]

4. Refinement of Board Independence and Disclosure Norms (2003–2004)

The N.R. Narayana Murthy Committee (2003)[12] built upon earlier reforms by strengthening the role and independence of boards, refining disclosure obligations, and mandating greater accountability in financial reporting. Clause 49 was correspondingly amended to reflect higher governance standards, aligning Indian practices more closely with international benchmarks.

5. Corporate Law Reform and Statutory Embedding (2005–2013)

A structural turning point emerged with the J.J. Irani Committee (2005)[13], which undertook a comprehensive review of Indian company law. The Committee advocated a shift from a

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[10] SEBI, Report of the Kumar Mangalam Birla Committee on Corporate Governance (1999) https://www.sebi.gov.in/sebi_data/commondocs/corpgov1_p.pdf

[11]. Department of Company Affairs, Report of the Naresh Chandra Committee on Corporate Audit and Governance (2002) https://dea.gov.in/files/other_reports_documents/chandra.pdf

[12] SEBI, Report of the N.R. Narayan Murthy Committee on Corporate Governance (2003) https://www.sebi.gov.in/reports/reports/mar-2003/the-report-of-shri-n-r-narayana-murthy-committee-on-corporate-governance-for-public-comments-_12986.html

[13] Ministry of Company Affairs, Report of J.J. Irani Committee on Company Affairs (2005) https://ibbi.gov.in/uploads/resources/May%202005,%20J.%20J.%20Irani%20Report%20of%20the%20Expert%20Committee%20on%20Company%20Law.pdf

prescriptive regime to a principle-based framework, with governance embedded into the core architecture of company law rather than treated as a listing-centric concept.

These recommendations culminated in the enactment of the Companies Act, 2013, which codified directors' duties, board processes, shareholder remedies, and accountability standards. Governance obligations were thus statutorily extended beyond listed companies, signalling a move towards entity-wide governance discipline.[14]

6. Contemporary Reforms and Consolidation (2017–Present)

The Uday Kotak Committee on Corporate Governance (2017) reflected the next phase of reform, focusing on board effectiveness, quality of disclosures, and enhanced accountability of promoters and management.[15] These reforms coincided with increased judicial scrutiny of governance failures, particularly in cases involving insolvency, fraud, and large-scale mismanagement.

Tribunals and courts have increasingly treated governance lapses as systemic risks, linking weak governance to corporate collapse and stakeholder harm.[16] Importantly, governance expectations today extend beyond listed companies, influencing unlisted companies, startups, and PE/VC-backed entities through contractual and judicial mechanisms.

Corporate Governance in Unlisted Companies

1. The Governance Gap in Unlisted and Closely-Held Companies

Corporate governance challenges are often most acute in unlisted and closely held companies. Unlike listed entities, private companies are not subject to continuous market scrutiny, analyst oversight, or extensive disclosure obligations. Control is typically concentrated in founders or promoter groups, and board processes tend to be informal. As a result, governance is frequently viewed as discretionary rather than structural, and is often addressed only when disputes arise or external capital is introduced.

This perception overlooks a critical reality: the absence of public market discipline increases, rather than reduces, governance risk. It has been well recognised that governance failures in private companies can lead to oppression, mismanagement, and abuse of corporate power, warranting judicial intervention even in closely held corporate structures.

2. Statutory Governance Framework Applicable to Unlisted Companies

Contrary to common assumption, corporate governance in India is not limited to listed companies. The Companies Act, 2013 embeds core governance obligations that apply

[14] Ministry of Company Affairs, Report of J.J. Irani Committee on Company Affairs (2005) https://ibbi.gov.in/uploads/resources/May%202005,%20J.%20J.%20Irani%20Report%20of%20the%20Expert%20Committee%20on%20Company%20Law.pdf
[15] SEBI, Report of the Kotak Committee on Corporate Governance (2017) https://www.sebi.gov.in/sebi_data/attachdocs/oct-2017/1509102194616.pdf
[16] *Innoventive Industries Ltd. v. ICICI Bank*, (2018) 1 SCC 407

equally to unlisted companies, including fiduciary duties of directors, requirements relating to board meetings and decision-making, regulation of related-party transactions, and remedies for oppression and mismanagement.

3. Investor-Driven Governance in Private Companies

In practice, governance in unlisted companies is shaped as much by commercial expectations as by statute. Private equity funds, venture capital investors, and strategic investors increasingly treat governance quality as a threshold investment criterion. These expectations are influenced by international benchmarks as mentioned earlier in this article.

Investors typically seek governance rights that enable oversight without interfering in day-to-day operations, including board representation, enhanced information rights, affirmative voting on reserved matters, and audit and compliance oversight. Weak governance structures often translate into valuation discounts, enhanced control rights, or delayed capital deployment.

4. Contractual Governance Architecture

Given the limited application of listing-based norms, governance in unlisted companies is largely implemented through contractual arrangements. Shareholders' agreements, investment agreements, and board charters function as the primary governance instruments, allocating decision-making authority, defining veto rights, and prescribing reporting obligations.

Indian courts have recognised the enforceability of such contractual governance mechanisms, provided they are consistent with company law and do not fetter statutory powers improperly.[17] As a result, governance in private companies is increasingly negotiated ex ante rather than litigated ex post.

5. Governance as a Value and Exit Enabler

For founders, early adoption of governance frameworks is not an investor-centric concession but a value-preserving strategy. Robust governance reduces transaction friction during fundraising, strengthens diligence outcomes, and enhances exit readiness in M&A or public listing processes. Conversely, governance gaps frequently emerge as material risks during due diligence, leading to re-pricing or deal restructuring.

<u>Conclusion</u>

Corporate governance is not a periodic compliance response but a **structural design choice** that shapes how corporate power is exercised, monitored, and restrained over time. As the Indian experience demonstrates, governance frameworks have evolved in response to market failures, investor expectations, and regulatory learning, converging on a central

[17] *V.B. Rangaraj v. V.B. Gopalakrishnan*, (1992) 1 SCC 160

objective—preserving trust in the corporate form. In this sense, governance operates as long-term control architecture rather than episodic legal compliance.

From a commercial standpoint, governance quality has become a decisive factor in capital access, valuation discipline, and transaction readiness. Institutional investors and strategic acquirers increasingly assess governance as a proxy for board effectiveness, risk management, and promoter discipline. Indian governance norms, informed by global benchmarks such as the OECD Principles of Corporate Governance, and reinforced through legislative and judicial development, now reflect this alignment between legal obligation and commercial expectation.

For founders and promoters—particularly in unlisted and closely held companies—governance is often misconceived as an external or investor-driven constraint. In practice, it performs a protective function. Clear allocation of authority, disciplined board processes, and transparent information flows reduce internal friction, mitigate disputes, and preserve enterprise value across growth stages. Governance failures, by contrast, tend to surface at inflection points such as fundraising, restructuring, or exits, where remedial intervention is both costly and disruptive.

Corporate governance is not static. As companies scale, diversify, and attract new stakeholders, governance frameworks must evolve accordingly. The responsibility for this recalibration rests with boards and shareholders alike. This article sets the foundation for the analyses that follow, which will examine how governance principles are operationalised through boards, shareholder rights, and contractual mechanisms in Indian companies.

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