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3 JAN, 2012, 05.00AM IST, MAULIK VYAS,ET BUREAU

Corporate governance issues too play spoilsport for fund flows

MUMBAI: Overseas investors' cold shoulder to India may not all be due to economic woes, but the steadily rising worries about corporate governance may be also playing a role.

Allegations of misuse of funds and not honouring agreements have began to crop up from across the country as many past assumptions on businesses turned sour. Companies that promised bountiful returns to investors stand ravaged.

Last year saw the arrest of the managing director of an education company for fraud, easing off of the doyen of micro-finance industry, a promoter of a tea compan accusing partner of diverting funds. All these may not be of the magnitude of [Satyam Computer Services](#), the biggest 7,000-crore corporate fraud in the country, but are getting prominent and are capable of hurting investor sentiment.

"Corporate governance and foreign direct investment into a jurisdiction have an important correlation," says [Ravi Singhania](#), managing partner of Delhi-based law fir Singhania & Partners. "The higher the level of corporate governance, greater the amount of [FDI](#) flows into the country."

Foreign portfolio investments in Indian stock and debt markets slowed down to \$8.2 billion in 2011 from the year-ago period of \$39.5 billion. Foreign direct investment, the indicator of long-term belief in the Indian economy, fell to \$1.2 billion in October 2011 from \$2.3 billion in the same month last year.

When 2+2 is not 4 Misuse of funds spotted at many companies	
Company	Corporate Governance Issue
Everonn	CBI had arrested P Kishore, MD of Everonn Education, for tax evasion of ₹116 crore in August 2011
SKS Microfinance	SKS Microfinance's founder and chairman Vikram Akula had to step down from the company board because of governance related issues in November 2011
KS Oils	Auditors have found a hole in the company's books running into hundreds of crores of rupees because of which the company had to delay its annual reports for the year ended March 2011
Warren Tea	The promoter of Warren Tea, AK Rujas, had filed an appeal against the company's chairman VK Goenka for siphoning of funds. As per the petition, they got to know about the same after an Income Tax raid in January 2011
Viom Network	Viom Networks, a telecom tower company, has hired consultant KPMG to probe into alleged misappropriation of funds in September 2011

While overall growth outlook is mostly responsible, unattended corporate governance issues could take India back to the 90s when most global investors avoided the country due to poor governance standards.

Regulations and companies have come a long way since, with even investors such as Calpers, which insist on high levels of governance, have begun investing here.

"Corporate governance or lack of it seems to be one of the top-mos concerns of foreign funds wanting to invest in India," says Pratibha Jain, partner, Nisith Desai & Associate.

"Lack of transparency coupled with series of scams without a strong response from the regulators to address the fundamental issues relating to corporate mismanagement in India, could have a negative impact on foreign investments into India."

Companies from Norway's Telenor to private investor Bain Capital are embroiled in controversies. Telenor's joint venture partner Unitech's founding

family member was behind bars for months for allegedly playing a role in loss to the exchequer in purchase of telecom licence. Bain accused its investee company Lilliput, maker of kids garments, of fudging accounts.

India ranks 134, out of 183 countries on the World Bank's index of 'Ease of Doing Business'.

Some hope could be revived if the proposed Companies' Bill is cleared by Parliament, since it has provisions that would strengthen the role and increase the responsibility of independent directors on the companies' board.

"The delays in the passing of the new Companies Bill have certainly impacted reforms which could have made India Inc more transparent," says [Pradip Khaitan](#) partner of Khaitan & Co.

"The proposed bill is defining the role of independent directors and auditors more clearly. Also, this proposed bill has a whistle blower policy which gives enough security to person who reveals any such corporate governance related irregularities."

The proposed new Companies Bill is significantly focusing on the role of independent directors, more accountability towards auditors of companies, facilitation of mergers and acquisitions and protection of minority shareholders. The new bill have provision to empower a tribunal to direct the company either suo moto or upon application by central government or any concern person to change the auditors in the case of any fraudulent action.

Also, there is a provision to blacklist the auditor for a period of five years from the date of such direction from the tribunal. While, for listed companies, there shall be at least one-third of directors to be independent ones.

Such independent directors shall be responsible for all act of omission that occurred with his knowledge or with his consent or connivance or where the director had not acted diligently.

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