The new Companies Act in India promises sweeping changes to corporate governance that aim to bring the developing economic giant and its businesses more in line with other large international capital markets. The Act is expected to boost mergers, help protect investors from corporate delinquencies and encourage foreign investment.

The new rules have far-reaching implications, most notably on the fiduciary responsibilities of the board of directors. They are designed to bolster independence and enhance corporate social responsibility. The Act can be seen as having two parts – the relaxation of rules around business growth, and a tightening of governance to ensure that growth is fair, legal and publicly monitored.

The Act was given presidential assent in September, replacing the 1956 legislation, and has been followed by a set of Draft Rules which contain provisions on the implementation of the new Act. While some of the legislation is effective immediately, other parts are subject to a phased roll-out.

More powers for the board

Under the new rules, the board has new powers to make decisions about: issuing securities within or outside India; diversifying the business; and approving amalgamation, merger or takeovers.

And more scrutiny

But with additional powers comes additional scrutiny. The Act demands a wider range of disclosures and requires the board to formally assume responsibility for key matters of governance, including:

- The risk management policy
- The ratio of each director’s remuneration to the median employee’s remuneration
- A formal code of professional conduct.

Other headline provisions place greater emphasis on gender equality and local communities. Companies are required to spend 2% of net profits on corporate social responsibility activities, for example. And they must appoint at least one woman to the board and one resident director. A “vigil” mechanism is also required to encourage and protect whistleblowers who report genuine concerns, but this does not apply to private limited companies.

Some apprehension

There has been some apprehension over aspects of the Act that are considered more stringent, or irregular. But the minister for Corporate Affairs, Sachin Pilot, emphasised that his department would revisit and clarify some matters, including mandatory auditor rotation. He called for further input from business and concluded that “the new Act and Rules will ensure less regulation...and will facilitate doing business in India more efficiently”.

But broadly positive response

The reaction from business has been broadly positive. “It reminds people at the helm of governance of their duty to act in good faith, in the best interests of the company, its employees, shareholders and the environment,” said Harinderjit Singh, a partner at PwC in India. He emphasised that many of the changes were relatively minor, adding that “self-monitoring” is effective but sometimes “needs a boost in the right direction from the regulators”.

“The new Act and Rules will facilitate doing business in India more efficiently.”

Sachin Pilot, Minister for Corporate Affairs, India