Augmenting the Role of the Board in Enhancing Transparency

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The key benefit of the corporate form was the divestiture of the ownership and management which paved way for professional management acting on behalf of the wider capital contributors. Such dichotomy resulted in the establishment of a special kind of principal-agent relationship between the shareholders and the directors. This relationship has been studied over the centuries by the jurists and the economists alike with a resulting deluge of not only academic literature but also legislative interventions.

The problem of information asymmetry

With the increasing size and influence of the companies, the key issue under discussion was agency costs and externalities of the decisions of the Board of directors and other officers of the company. The crucial factor of this problem was the information asymmetry between the directors and the shareholders. Such information asymmetry led to decisions which protected the directors at the expense of the shareholders.

The evolution of the corporate legislations points out that a large portion of the provisions are aimed at curing this information asymmetry. There are a range of provisions which require certain disclosures coming from the directors as well as certain key managerial persons to the company. These disclosures are basically with reference to their interests in other entities and they are of personal nature. However, a wider view of the disclosures is required to be taken, as discussed below.

The concept of 'transparency'

Transparency, though generally known and understood, eludes a precise definition which can outline its borders. The concept has multiple dimensions including the moral ones. While the moral dimensions are to be ignored for the purpose of this article, the linguistic interpretations and its subsequent morphing into a normative concept results in different conceptions in the minds of different persons.

The linguistic interpretation of the concept implies an object which is capable of being viewed or seen through by a subject. The key drawback for transparency in the corporate setting is that the person who knows decides whether to tell the other or not and if yes, then how much to tell.

Transparency in Corporate Governance

There are two aspects of transparency in a corporate structure: towards shareholders and towards the other stakeholders. The transparency may be ranked on various parameters like the transparency in the financial disclosures, legal compliances, labour practices, supply chain, environmental impact, political contributions or engagement, anti-corruption measures, human rights, and the like.

Transparency is perhaps the cornerstone of all the principles and practices of corporate governance. The G20/OECD Principles of Corporate Governance also recognise the importance of transparency, though from the perspective of the investors in listed entities. The recommendations made therein are with respect to better dissemination of the existing disclosure requirements and do not necessarily require any additional legal right in favour of the shareholders.

Tailoring the transparency requirements to a type of entity

A 'one-size-fits-all' conception of transparency is unlikely to succeed in its implementation. It should be noted that though there are several provisions for a listed entity which require qualitative and quantitative disclosures, the same may also result in an information overload. On the other hand, very few disclosures are required under the Board's report and the financial statements for the unlisted companies. Such disclosures tend not to provide any clear

guidance as to the future direction of the business.

Further, frequent changes in the disclosure requirements for a company (as anecdotally observed in cases of private companies) results in establishing an uneven framework of transparency principles.

Such a lack of a proper channel to gather information results in the proliferation of inaccurate and unsubstantiated reports through social media. The omnipresent experts of these platforms lead the vast majority to make sub-optimal decisions.

Establishing the 'Right to know'

In a typical principal and agent relationship, the principal has an established right to know the actions of the agent as he is going to be ultimately responsible for the same. Though the shareholder-director relationship is not strictly resembling the principal-agent, certain similarities can be readily observed. Under the present scheme of the Companies Act, 2013, the shareholders have numerous other rights ranging from requisitioning a general meeting to filing for reliefs in cases of oppression and mismanagement whenever certain decisions of the directors are thought to be detrimental by them.

However, there is no right with the shareholders to call for information related to the business of the Company. Such an absence of what could be otherwise thought of as a precursor to the rights mentioned above is baffling.

There are certain other classes of companies like Nidhis and Producer companies whose members (who are usually large in number and have both financial and business interests in the success of the company) are left to fend for themselves without any clear right to know about the business of the company. Though the route of establishing such 'right to know' is available under the Articles of Association, practically the scattered nature of shareholders means that the bargaining power remains distributed.

Legislative mandate v. stakeholderism

The next line of argument would be whether a legislative mandate shall be formulated where the shareholders get a right and the Board is simultaneously placed under a duty. The present legislation, though having certain duties for individual Directors and certain limits on the collective powers of the Board, there are no duties towards enhancing transparency. Such provisions can well be drafted and included without upsetting the overall scheme of the corporate legislations.

Further, the audit mechanisms which were likely to institute a strong quasi-regulatory check are yet to live up to the promise. The lack of proper enforcement of auditing standards leads to abrupt outbursts of remarks and qualifications without the sustained checks required to reap the real benefits.

A few aspects are required to be consulted before the same can be decided. The principles of corporate legislations, as thought of by a select clique of academicians, should be permissive of the same. The common argument from such vantage point is that certain provisions in the corporate laws are an overreach and fall well outside the desired remit of the corporate laws. However, as this right has the basic intent of reducing agency costs and increasing the efficiency of the corporate form, it shall not fall foul on this touchstone.

The goal seems to be too important to be left to stakeholderism which is proved to be futile by certain reputed academicians. At the same time, the balance of the provisions needs to be finetuned to make sure that the compliance costs do not mar the cost-benefit analysis of such provision. Further, a few exceptions regarding confidentiality of the business secrets can be carved out to protect the business interests of the Company.

Designing a way forward

The aim here is to engage in and encourage a debate about the possible rights of the shareholders and other stakeholders to force the company to shed more light on its affairs. Certainly, this shall not be a panacea but shall at least be a potent weapon in the hands of shareholders and other select stakeholders.

To conclude on a lighter note, one may recall a famous scene from 'Yes, Prime Minister' where the Cabinet Secretary Sir Humphrey Appleby elaborated his 'need-to-know' requirements as "I need to know everything. How else can I judge whether or not I need to know it?". A kindred right, though not as expansive or generous, needs to be thought of for the benefit of various stakeholders.