
Case Study on Larsen and Toubro and GMR Infra Ltd and their Corporate Governance disclosures based on Narayan Murthy Corporate Governance Report

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Abstract

This case study aims at studying the recommendations on Clause 49 of Corporate Governance report by Narayan Murthy Committee report released in the year 2003. All the issues brought up by the committee have been studied in detail and a comparative analysis has been done on how closely two leading companies in the infrastructure sector – Larsen & Toubro and GMR Infra, adhere to the suggestions and the recommendations in the Narayan Murthy report. Annual reports and corporate governance reports, for the financial year 2015-16, of both the companies are read through thoroughly. Major issues raised in the committee's report are extracted and both the companies are put through an acid test to check how well the recommendations are followed by them. The results suggest that L&T is more compliant and transparent, however GMR Infra provides a more concise and reader – friendly corporate governance report in comparison to L&T. Most of the disclosures have been clearly stated in the reports. Any deviation in the normal course of work or transactions that are not on an arm's length are referred to in notes to the financial statements. Whistle blower policy and code of conduct manual for both the organizations are in place. The study has been enriched with suggestions and comments on the transparency of the annual report and corporate governance report (2015-16) released by the companies.

Key words Corporate Governance , Narayan Murthy report, compliances

Introduction

The essence of corporate governance lies in the framework it provides for successful relationships amongst company's senior management, board members, directors, shareholders, internal and external auditors and stakeholders. The guidelines help in attaining the goals and objectives of the company smoothly and at the same time provides a structured mechanism for monitoring the company's performance. Transparency of internal controls and operations, corporate responsibility, accountability of management and members of the board to the shareholders and investors is the key to effective corporate governance. Good Corporate governance not only adds value to the company's brand name and performance but also provides mechanism for measuring and minimizing risks that an organization can face.

The case is a study on the corporate governance report of two of the leading infrastructure companies – Larsen and Toubro and GMR Infra. It is a detailed analysis of the extent to which both the companies adhere to the recommendations in the Narayan Murthy report, followed by suggestions and recommendations on the basis of the review done.

Company Profile

Larsen and Toubro

About: L&T is a company that is doing great work in the field of technology, engineering, financial services, manufacturing and construction. L&T caters to critical needs of various global companies, spreading over sectors like Power, Infrastructure, Hydrocarbon Industries and Defence. It meets the needs of customers spreading across 30 countries (worldwide).
Founder: Søren Kristian Toubro and Henning Holck-Larsen
Year: 1938
Headquarters: Mumbai
Market Cap: Rs 1.39 Trillion
Corporate Governance: Every division of the company’s businesses is known for its professionalism and meeting high standards of corporate governance.

GMR Infra

About: GMR Group, initially, was into Agri-based industry. The group gradually created its mark in the Infrastructure space. It has been doing excellent work in areas like Airports, Highways, Urban Infra, and Energy. The company also has a world class presence with infra operating assets and projects in various countries like Turkey, Indonesia, Maldives, Singapore and South Africa.
Founder: Grandhi Mallikarjuna Rao
Year: 1978
Headquarters: Karnataka
Net Revenue: Rs 82.4 Billion
Corporate Governance: Principle followed by GMR 'Achieve right results by right means'. The Group strictly abides by legal guidelines and attempts to satisfy its stakeholders following a steadfast approach.

Business Group	L&T Group	GMR Group
Sector	Infrastructure Developers & Operators	Infrastructure Developers & Operators
Incorporation Year	1946	1996
Chairman	A M Naik	G Mallikarjuna Rao
Managing Director	S N Subrahmanyam	Kiran Kumar Grandhi
Company Secretary	N Hantharan	A S Cherukupalli
Auditor	Sharp & Tannan/Deloitte & Haskins & Sells LLP	S R Batliboi & Associates LLP
Registered Office	L&T House,	Naman Centre 7th Flr P No C-31,
Face Value (Rs)	2	1
Stock Exchange	NSE, BSE	NSE, BSE
Listing	London,Luxembourg,MCX-SX,Mumbai,NSE	MCX-SX,Mumbai,NSE
Tot.Employees	43354	766

N.R. Narayana Murthy Committee Report

The N.R. Narayan Murthy Committee, formed under the Chairmanship of Shri N. R. Narayana Murthy (Chairman of Infosys Tech. Ltd.) had appointed a pool of members from across the industries. Academicians, elite industry heads, public accountants and people from financial press and other forums constituted the committee.

Highlights of the report's mandatory recommendations:

- **bolstering responsibilities of audit committees** – It should have an idea and knowledge of the disclosure of financial information, AC must meet four times in the periodic year and the gap between two consecutive committee meetings should not be exceed four months, 1/3rd members including 2 independent directors must be present
- **improvising the quality of disclosures (financial), related party transactions' disclosures, including proceeds from initial public offerings (IPO)** – No records but summary statement of RPT should be included, material individual transactions that deviate from the rules of normal transaction or the rule that says transactions have to be on an arm's length, must be reported to AC.
- **executive boards (corporate) should check and disclose threats and risks related to business in the periodic reports**- Every quarter, a report shall be presented to the Board of Directors. It will cover the risks in business that the company documenting may face, techniques and ways to mitigate risks, limitations (if any), to the extent of risk that a corporation can take. The document has to be officially verified and approved by the board's directors.
- **adoption of formal codes of conduct and the position of nominee directors**- It is the responsibility of the board to ensure a code of conduct is laid down and followed. Means for company employees to be able to report unscrupulous or fraudulent behaviour, cases of frauds or non compliance to the company's code of conduct or should be in place.
- **disclosures relating to remuneration/compensation of non executive directors and approval of shareholders** – Board must fix the compensation of non-executive directors (including independent directors) and should further seek approval from stock holders during general meetings. An upper cap is put on the stock options that are accorded to the NED in total.
- **whistle blower policy** –Company policies must provide provisions for protecting "whistle blowers" from any unfair treatment or any form of employment practices that are prejudicial.

Highlights of the report's non-mandatory recommendations:

- corporate to move closer to having non qualified financial statements
- following a system of training and development of the members of the board
- evaluating board members' conduct/performance

As per the Narayan Murthy team, the recommendations provide standards for 'good governance' to be incorporated in a system. Implementation of these recommendations through the regulatory framework designed by SEBI shall bolster current practices in existence and help discover a way to minimize corporate failures.

Analysis of Corporate Governance in Larsen & Toubro and GMR Infra

1) Independent Director

CLAUSE	GMR	L&T
Independent Director is non-executive director who: a) doesn't share any material relationships or pecuniary associations with the company, including senior management and promoters of the company, holding company or subsidiaries b) is not a substantial shareholder of the company c) isn't a material supplier, customer or doesn't provide services to the company	Compliant - ID don't have any pecuniary relationship and are material suppliers/customers	Compliant - ID don't have any pecuniary relationship and are material suppliers/customers

2) Compensation paid to Non Executive Directors

CLAUSE	GMR	L&T
Compensation paid to NED (inclusive of independent directors) should be decided by the BOD and further seek confirmation of the stakeholders in general meetings	The BOD decides the compensation but no mentioning regarding the shareholder's approval	No mentioning regarding the shareholder's approval

3) a) Meeting of Audit Committee

CLAUSE	GMR	L&T
Meetings of the committee must be, a minimum of 4 times in a financial year and the gap between consecutive meetings must not exceed four months. One third members of the audit committee should attend the meeting wherein at least two independent members must be present	Compliant - Met 6 times in the year 2015-16. All the 3 members (and ID) attended the meeting . 1 member was included in the team post 10 th Feb 2016 didn't attend any meeting.	Non Compliant - Met 8 times in the year 2015-16. No mentioning about the number of members who attended the meeting.

4) b) Review of Information by Audit Committee

CLAUSE	GMR	L&T
Audit Committee compulsorily will review the following: 1. MDAR - Management discussion and analysis report, explaining financial condition and consequence of the operations 2. A summary and not a detailed record of related party transactions that is submitted by management 3. Letters by the management and on internal control weaknesses released by internal or even external auditors 4. Audit reports on internal control weaknesses 5. The AC shall appointment, remove, re-appoint, review terms of compensation/remuneration of chief internal auditor	Compliant - GMR's Audit Committee reviews all the information	Compliant - L&Ts Audit Committee reviews all the information

5) **Disclosure of Accounting Treatment**

CLAUSE	GMR	L&T
If there is a deviation of non affirmation to any accounting standard, the auditor must justify the same and disclose the reason to qualify the report. An explanation should be provided by the management in the notes to financial statements.	Compliant- Deviation from accounting standards and policies are disclosed in the notes to the financial statements	Compliant- Exceptions are mentioned in the notes to the financial statements.

6) **Risk Management Disclosure**

CLAUSE	GMR	L&T
Each quarter, a report is presented to the management by the Board of Directors detailing the risks in business that can be faced by the company, ways to address and mitigate the risks, and all the limitations to define the extent to which a corporation can take risks. The Board has to formally approve the above mentioned document.	Compliant- risk management framework of GMR explains the applicability, risk management structure of the organization, linkages, coverage, processes, etc	Compliant- It has in place a risk management policy to inform the board members about risk management and mitigation procedures. Regularly reviews are done.

7) **Remuneration of Directors**

CLAUSE	GMR	L&T
All elements of compensation package/remuneration of individual directors should be summarized under categories like salary, bonus, stock options (with limits), benefits, pension, etc	Compliant- All elements of remuneration are mentioned	Compliant- All elements of remuneration are mentioned

8) **Whistle Blower Policy**

CLAUSE	GMR	L&T
1. A mechanism is employed to report, to the concerned authority, about unethical behaviour, fraud, deviation from following ethical policy or breach of code of conduct laid down by the company 2. The whistle blowers must be safeguarded from being victimized on reporting unethical behaviour 3. Audit Committee should periodically review the existence and functioning of the mechanism	Compliant- Company provides a mechanism against victimization of employees	Compliant- Company has a vigil mechanism to provide for adequate safeguard for employees who report unethical cases.

9) **Related party Transaction Disclosure**

CLAUSE	GMR	L&T
A not so detailed summary statement of the transactions with related parties in ordinary course/flow of business has to be presented within regular intervals to the AC	Non Compliant- Summary statement is not mentioned in CG report. However, details are mentioned in note 32 (Notes to Financial Statements)	Compliant- It provides info on nature and volume of transactions. Audit Committee reviews statement of related party transactions

10) **Adoption of formal Code of Conduct**

CLAUSE	GMR	L&T
A code of conduct should be in place for the members who are on board and the senior management as well	Compliant- A formal code of conduct exists and is posted on company's website (www.gmrgroup.in)	Compliant- A formal code of conduct has been laid down but information is unavailable

11) **Training to Board Members**

CLAUSE	GMR	L&T
Encouraging the company to provide training to its board members on business model and the risk parameters of the company.	Non Compliant – Not mentioned in the CG Report	Compliant –The company has provided training programs to its employees.

12) **Subsidiary Companies**

CLAUSE	GMR	L&T
Subsidiary Companies: 1. The composition and provisions of the Board of Directors of the listed holding companies should be the same as that of the material non-listed Indian subsidiaries. 2. A minimum of one independent director on the BOD of the parent company and the BOD of a subsidiary company (material, non listed and Indian) should be common. 3. The Audit Committee of holding company (if it is listed) shall also review the financial statements. 4. The minutes of the meeting of the unlisted subsidiary company shall be placed for review by the members on the board.	Non Compliant: GMR discloses that BOD performs regular review of subsidiary companies but no info regarding ID of subsidiary and parent company is mentioned	Non Compliant : No information is given about subsidiary companies in the CG Report

Findings

1. L&T has been more regular in conducting audit committee meetings and reviewing financial statements, related party transactions, appointment and reappointment of members, etc.
2. Information about the term of office of Directors is not available in the CG report of both GMR Infra and L&T.

3. Both, L&T and GMR Infra meet the criteria of the number of members in the audit committee, remuneration and/or nomination committee, condition on the number of Independent Directors and the number of and gap between meetings in a financial year, etc. as per the report.

4. Both the companies have been following the clauses by Narayan Murthy Report very closely except a few deviations as mentioned in the analyses.

5. CG report for GMR is more specific and gives minute details about dates of BOD meetings, subsidiary companies, code of conduct, etc. However, L&T is better in terms of training board members, related party transaction disclosures, etc.

Conclusion

The analysis shows that L&T is more compliant than GMR Infra. However, considering the available information, GMR Infra has presented the information in a clearer and elaborate manner in comparison to L&T.

Recommendations

On studying the corporate governance reports of GMR Infra and L&T, the following recommendations are made:

1. The CG report of L&T is not as structured as that of GMR. One needs to read through the entire report and refer to website to get a clear picture of different sections. Thus, it can be more precise and clear.

2. Some information on Related Party Transactions, members who attended the Audit Committee meeting, selection procedure of Independent Directors should be openly stated in the report.

3. Training and development programs by organizations play a significant role in the growth of the company and the individual per se. Thus, they should be mentioned in the CG report.

4. An immediate meeting should be organized after taking a new member on board in any of the committees.

5. GMR should provide training to board members often and state the same in CG report.

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