

## Satyam scam: Lessons for Corporate Governance

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### ABSTRACT

The Satyam scandal dubbed as India's Enron is one of the largest accounting frauds in the country's corporate history. B.Ramalinga Raju, founder and chairman of Satyam Computer Services Ltd., the fourth leading IT services firm, declared on January 7, 2009 that his company had been faking its accounts for years, exaggerating revenues and overstating profits by \$1 billion. This article examines the Satyam scandal and explains what happened, why and who is to blame. Satyam's emergence from a local to a global traded conglomerate is traced, followed by the events in the aftermath of the scandal. The paper concludes with the proposed regulatory prescriptions encapsulated by the new code created by India's Ministry of Corporate Affairs, with suggestions proposed by the Parliamentary Standing Committee. These prescriptions are likely to be introduced in the impending Budget session of Parliament. They relate to the functioning of independent directors, enhanced pace of disclosures, conduct of audit and improved transparency in governance mechanisms.

**Keywords:** Corporate Governance, Satyam Computer Services Ltd., Price Waterhouse, scandal

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### Introduction

By Ramalinga Raju, founder and chairman of Satyam Computer Services Ltd., saying publicly on January 7 2009, that his firm had been misrepresenting revenues and overstating profits by \$1 billion, is a case of corporate *mis-governance* and accounting malpractice. Specifically, Ramalinga Raju (Raju) admitted that Satyam's balance sheet included ₹.7,136 crore (almost \$1.5 billion) in non-existent cash and bank balances, accumulated interest and misstatements. India Knowledge @ Wharton (2009) reports that Satyam had inflated revenues in the second quarter 2008 by ₹.588 crore (\$122 million) to ₹.2,700 crore (\$563 million) and operating margins were below 10 percent the declared ₹.649 crore (\$135 million). Indeed, the Satyam scandal has no parallel in the history of Indian corporate experience. Satyam has become an ongoing saga where the investigation and auditing are still carried out by RBI and SEBI.

A firm with positive corporate governance practices, commits & espouses ethical practices across its entire value chain and with all stakeholders - investors, employees, clients, vendors and regulator.

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This article examines the Satyam Computers scandal from the perspective of corporate governance, and explains what happened and why. We look at who is to blame for the scam which is labeled as 'India's Enron' (Economist,2009), the stakeholders and their role with reference to issues of disclosure and mis-governance. The paper concludes with the regulatory reforms proposed in the aftermath of Satyam.

**Table 1**

***Inflated figures as on 30 September 2008***

- *Inflated figures for cash and bank balances of ₹5,040 crore (US\$1.09 billion) as against ₹5,361 crore (US\$1.16 billion) reflected in the books*
- *Accrued interest of ₹376 crore (US\$81.59 million) which was non-existent*
- *Understated liability of ₹1,230 crore (US\$266.91 million)*
- *Understated debtors' position of ₹490 crore (US\$106.33 million) (as against ₹2,651 crore (US\$575.27 million) in the books)*
- *Inflated staff by 12000(Actual were 40000)*

**Source :** <http://www.moneycontrol.com/financials/satyamcomputerservices/balance-sheet/SCS>

**What Happened and Why?**

The Satyam<sup>1</sup> scandal broke out in the backdrop of the economic recession in 2008. As stock markets worldwide caved in, the Indian stock market, Sensex, also fell from 21000 to below 8000 between January-October 2008. Cash withdrawals in large amounts caused the discovery of a number of cases of financial fraud, particularly in the US.

Ironically, despite the economic upheaval in key markets, Satyam showed positive results with a net income of \$132.3 million in October 2008, a 28 percent increase year-on-year in the second quarter (<http://www.thefreelibrary.com>). Post-October 2008 onwards, the firm faced difficulties on several fronts which snowballed into the mega crisis.

Winkler (2010) spells out the chronological sequence of the events leading to the scam:

- ✓ In October 2008, the World Bank fired Satyam as a supplier and enforced an eight-year ban against the firm. The World Bank charged Satyam of fitting spy systems on its computers and appropriating assets.
- ✓ In October 2008 at a conference call on Satyam's September 2008 quarterly earnings, Kawaljeet Saluja, an insightful stock analyst from Kotak Securities, drew attention to the huge cash balances in non-interest bearing bank accounts. Saluja expressed apprehension about the balances and conveyed reservations about the accuracy of the numbers (Live Mint, 2009). A warning largely discounted by investors riding high on the company's declared positive earnings and revenue growth.
- ✓ On December 16 2008, Satyam's Board of Directors unanimously endorsed the purchase of Maytas Properties and Maytas Infrastructure, two property development and infrastructure construction firms for \$1.6 billion.

- ✓ Institutional Investors were outraged, stating they would fervidly oppose the deal going through. Maytas Properties and Maytas Infrastructure were promoted and controlled by Raju's family and unrelated to the firm's prime field-Information Technology <sup>2</sup>.

The deal was perceived as daylight robbery as Raju's family held a bigger stake in these 2 Firms than even in Satyam!

- ✓ Sparking a strong negative reaction, analysts placed sell recommendations on the Satyam stock. The shares pummeled on the New York Stock Exchange and NASDAQ with Satyam shares falling by nearly 10 percent.
- ✓ On the same day, December 16 2008, the board of directors swiftly reconvened and cancelled the proposed venture.
- ✓ By December 29, 2008, four of the five non-executive directors on the Board all outstanding figures in industry, resigned hoping to regain their credibility (Banerjee, 2008).
- ✓ On December 30 2008, Forrester Research counseled clients to stop doing business with Satyam because of the fear of widespread deceit.
- ✓ Post-december fiasco, Satyam appointed DSP Merrill Lynch for advice to augment shareholder value. On January 7 2009, merely hours before Raju divulged the fraud, Merrill Lynch wrote to the Securities and Exchange Board of India-SEBI(India's SEC),stating that it was pulling out from its engagement with the company as it came across accounting irregularities.
- ✓ On January 7 2009, Raju divulged in a confessional letter to Satyam's Board of Directors that he had been manipulating the company's accounting figures for years! Satyam had ₹7,136 crore (nearly \$1.5billion) in non-existent cash and bank balances, accrued interest and mis-statements (Express India, 2009).
- ✓ Instantaneously, following Raju's admission, the company's share price plunged 77 per cent to ₹30 (60 cents), a mammoth drop from its 52-week high of ₹544 (\$11.35).
- ✓ On January 10 2009, Satyam's board of directors called an emergency meeting to address the company's rapidly worsening reputation.

The fissures in Satyam were widening, could not be glossed over and finally imploded.

Table 2

***Satyam's emergence from locally controlled corporation to globally traded conglomerate***

*Raju formed Satyam Computer Services Ltd. with fewer than 20 employees in 1987 in the southern city of Hyderabad. The company initially started off focusing on technology, constantly reinventing itself.*

*In 1991 Satyam issued an initial public offering on the Bombay Stock Exchange and experienced success. The firm grew rapidly in the 1990s and 2000s riding on India's growth as a global outsourcing hub.*

*Satyam specializes in information technology, business services and computer software and in time became the fourth largest technology outsourcing corporation in India, nipping on the heels of India's "Big 3" Information Technology giants- TCS, Infosys and Wipro.*

*Satyam provides solutions to approximately 185 Fortune 500 companies and was listed on both the New York Stock Exchange (NYSE) and the Bombay Stock Exchange (BSE). At its peak, Satyam engaged 53,000+ employees with clients in 67 countries.*

*Satyam won several awards for innovation, (and ironically) for governance and corporate accountability.*

- *2007, Ernst & Young prized Raju with the "Entrepreneur of the Year" award*
- *April 14, 2008, the MZ Consult's award for being a leader in India in corporate governance and accountability*
- *September 2008, the World Council for Corporate Governance gave the "Global Peacock Award" for global excellence in corporate accountability*
- *2007, the American Society for Training and Development (ASTD) named Satyam the 'BEST' company in the world for workplace learning and development*

**Who is to be blamed?**

Satyam was often cited as an exemplar of India's rising achievements starting as a local home-grown business to a globally-traded conglomerate. Raju himself in his home state of Andhra Pradesh was feted and heralded as the local (Andhra) boy who had made it big. The company won a number of accolades and awards. In fact on September 2008, one month prior to the scam breaking out, the World Council for Corporate Governance honored Satyam with the "Global Peacock Award" for global excellence in corporate accountability! Regrettably, five months later, Satyam became the centerpiece of a gigantic accounting fraud.

Indian authorities held Raju as the principal individual responsible for the scam. The following individuals were also held accountable:

- ✓ Raju, and his 'inner circle' - his younger brother B.Rama Raju, Satyam Managing Director and CEO (also a co-founder), Srinivas Vadlamani, the Chief Financial Officer and V. S.

Prabhakar Rao, the global head of internal audit were accused with criminal charges of fraud.

- ✓ Satyam's auditors a "Big Four" auditing firm Price Waterhouse Coopers (PWC), bear some blame because of their failure to detect the fraud.
- ✓ Satyam's Board of Directors who are responsible to monitor the firm's ongoing activities and to have a say in its governance.
- ✓ The ownership structure of family-run Indian businesses.

### **How did Raju and his company associates commit the fraud?**

Raju and V S Prabhakar Rao, the global head of internal audit employed varied methods to commit the scam.

- ✓ Raju made use of his personal computer to generate several bank statements to advance the fraud
- ✓ Faking the bank accounts to inflate the balance sheet through balances that were non-existent
- ✓ Blowing up the income statement by declaring interest income accrued from the false bank accounts
- ✓ Fabricating 6,000 false salary accounts and appropriating the funds once the firm deposited them

Raju himself acknowledged that the accounts manipulation began small, but over time reached "unmanageable proportions." Invoking the special place that the tiger holds in the Indian mind-space, he stated, "It was like riding a tiger, not knowing how to get off without being eaten." The aborted Maytas acquisition was the last effort to plug the conjured assets with valid ones.

Raju involved crucial company insiders to carry out the fraud. Prabhakar Rao ,Satyam's global head of internal audit added to the manipulation by:

- ✓ Generating phony client identities and producing fake invoices against their names to increase revenue
- ✓ Falsifying board resolutions and unlawfully acquiring loans for Satyam
- ✓ Ensuring that the money raised in American Depository Receipts ("ADRs") within the US never figured in the balance sheet
- ✓ Therefore Raju along with his brother B.Rama Raju,Satyam MD and CEO (also a co-founder),the CFO , Srinivas Vadlamani, and the global head of internal audit, V .S. Prabhakar Rao were responsible for engineering the fraud .

### **The role of Auditors....**

Price Waterhouse Coopers ("PWC") a Big Four auditing firm reviewed Satyam's books for over 8 years, from June 2000 till the unearthing of the scam.

PWC was criticized severely for the following reasons:

- ✓ Failure to detect the fraud
- ✓ Not applying due diligence in authenticating high-value items

- ✓ Not questioning the \$1.04 billion stated on its balance sheet as non-interest bearing deposits
- ✓ Not inquiring for simple reconciliation statements of fixed assets, bank accounts and client financial records and corroborating independently these statements with the banks

(The bankers comprised Bank of Baroda, BNP Paribas, ICICI, HDFC, Citi Bank, HSBC. Not a single bank on its part, enquired about the details in the company's balance sheet).

"Paying the Price: Satyam's auditors face plenty of questions" published in India Knowledge@Wharton highlights the auditor's dilemma (India Knowledge @ Wharton, 2009). The auditor is required to authenticate the financial statements presented by the firm-the balance sheet, profit and loss account and the cash-flow statement. While the auditor has to exercise 'due professional diligence' and have an approach of 'professional skepticism,' he is not required to have an investigative stance, unless there is cause for doubt.

While PWC avowed that it executed Satyam's audit in line with the accounting standards, the broad implication is that they were either inept or were complicit in the scam.

**Table 3**

***Not an isolated case...***

*PWC's experience at Satyam Computers is not the first encounter with corporate scandals in India and indeed across the globe. The following instances bear this out...*

- *2003, a new-generation private Indian bank, Global Trust Bank (GTB) caved in following a stock-rigging scam conceived by Ketan Parekh, a Mumbai-based dealer. PWC affiliate Lovelock and Lewis was the auditor and declared a net worth of US 480 million for FY March 2002. Shortly afterward, an investigation by the Reserve Bank of India (RBI), India's central bank showed a negative net value.*
- *2001, PWC was associated with the accounting scam at DSQ Software in India.*
- *May 2006, PWC's affiliate in Japan Chuo Aoyama, was suspended by the Financial Services Agency, following a suspicious audit of cosmetics firm Kanebo. Three accountants in the company purportedly aided with the fraud and raised the earnings by almost \$1.9 billion.*
- *July 2007, PWC consented to pay \$ 229 million to resolve a class-action lawsuit brought by investors of the US conglomerate Tyco International Ltd. over a multibillion dollar accounting scam.*

*The list goes on....*

*Source: <http://en.wikipedia.org/wiki/PwC>*

Post- Satyam debacle, lawsuits have been filed in the US with PWC as the defendant. Two partners of PWC, Srinivas Talluri and Subramani Gopalakrishnan have been accused by India's premier intelligence agency, Central Bureau of Investigation (CBI). In fact, in both PWC-tainted Indian cases

as well as in Satyam, PWC's partner Gopalakrishnan was signatory to the audit report .It was only in the final Satyam report that Talluri was the signatory(Mukerjee.R. and Shree,S.2009). Since the scam broke out, Subramani Gopalakrishnan has retired from the company on attaining the mandatory retirement age; while Talluri remains on suspension.

### **Responsibility of Directors...**

The board of directors is required to actively monitor the company-a fact which is not borne out by the case.. Satyam's Board of Directors consisted of nine members, inclusive of five independent directors as required by SEBI. The non-executive members comprised Krishna Palepu, Harvard Professor and Corporate Governance expert, M.Rammohan Rao,Dean of the prestigious Indian School of Business (ISB),Hyderabad,Vinod Dham,widely acknowledged as the"father of the Pentium chip" and presently managing partner of NEA Indo-US Fund and New Path Ventures, Santa Clara,California and Mangalam Srinivasan, business consultant and advisor to Harvard's Kennedy School of Government.

The lack of scrutiny and oversight of the board is attributed to the individual stature of the independent directors in the business world.

The board did not pay heed to the following signals:

- ✓ Raju decreasing his holdings in Satyam from 15.67 per cent to 2.3 per cent during 2005-06 to 2009 at the time of the exposé.
- ✓ The firm intending to invest \$1.6 billion in realty, an unrelated diversification,when HCL had just attained Axon to compete with Satyam ,a major implementer of SAP systems worldwide!
- ✓ Not questioning whether the unrelated diversification proposal is the right decision for the corporation ,given the strong family association.

Concerns have been raised about the working of Satyam's Board of Directors.

- ✓ The board did not have a single financial expert as revealed in the company's regulatory filings with SEC in 2008.
- ✓ Non-attendance by non-executive directors such as Palepu, who stated, that he was not present at the board meetings when the Matyas proposals were discussed.
- ✓ The Board could not exercise independence in its functioning due to the concentrated corporate control.
- ✓ Raju's partiality to appoint people from his same neck of woods, hometown, extended family and home state as directors , employees.

Consequently , given the secrecy and tight control by Raju and his cohorts ,the company did not have any whistle-blowers to raise an alarm. Raju himself blew the whistle! The ex-cofounder and chairman seems to be the lone corporate fraudster to have confessed his transgression – falsified accounts, overstated revenues, fictionalized profits, faked bank deposits and audaciously protracting it for seven years!

### **Shareholder involvement and activism?**

The climate of shareholder involvement seems to be characterized by:

- ✓ Tight control by the principal promoters

- ✓ Lack of information flow and transparency
- ✓ Subtle stifling of shareholder involvement and activism

In fact, investor activism in India is by and large passive. The Satyam case seems to be the first time shareholder activists have played a proactive role in India by resisting the board's resolution in attaining Matyas Properties and Maytas Infra. This rare incident led to the disclosure of frauds being committed by the principal promoters.

### **Ownership structure of Indian Businesses**

Analysts contend that the ownership structure of Indian businesses contributed to the Satyam scandal. On February 6 2010, the Indian government disclosed that its serious fraud office is investigating 325 companies embroiled in the scandal perpetrated by Satyam's ex-chairman, B. Ramalinga Raju, and one of his brothers (The Economist, 2009).

In fact, in the 1990s, almost one-third of Indian firms belonged to large business groups, run and managed by rich families or business "promoters." These business promoters organize their businesses as a pyramid construct which involves holding a number of diverse business lines and treating them as one division, transferring funds from one unit to another as required. Within this structure, the control group can "tunnel" the funds from firms at the base of the pyramid (where their stake is low) to the peak (where their stake is 51 per cent). The family's "control rights" may surpass their equity by a large margin. Thus, while the governance issue in the Anglo-Saxon model seeks to restrain the management, in India the problem is of disciplining the principal shareholder and defending the minority shareholders.

While Satyam does not conform to the pyramid structure, it is a case of control surpassing ownership. The firm had grown from a small family company to a corporation with 218,000 shareholders. However, despite Raju's family stake declining to 5 per cent by January 2008, the family's "control rights" were clearly evident. The ownership pattern results in the promoters being all dominant making even outstanding Independent Directors, as Vinod K Dham, Mendu Rammohan Rao, Krishna G Palepu, Mangalam Srinivasan... not of independence.

### **The Aftermath....**

The aftermath of the Satyam scam can be summarized in a series of sequential events:

- ✓ Indian stock market fell drastically
- ✓ Indian authorities swiftly began an investigation and followed criminal actions that ensnared Raju and key Satyam executives.
- ✓ Indian authorities arrested and charged the company's auditors Price Waterhouse Coopers, with fraud.
- ✓ The Institute of Chartered Accountants of India (ICAI) ruled that the CFO and Auditor was guilty of professional misconduct.
- ✓ A number of civil charges were filed in the US against Satyam by the backers of its ADRs, while both civil and criminal litigation are in process in India.
- ✓ The Indian Government restored confidence by appointing new board members who met with bankers, accountants, lawyers and government officials to work towards a solution that would avert the collapse of the firm.

- ✓ Satyam successfully emerged from the catastrophe through an asset sale by Tech Mahindra as the winning bidder in 2009. Tech Mahindra is the IT arm of Mahindra and Mahindra.

The financial details post- Mahindra Satyam takeover reveals the stark differences in specific financial parameters. Annexure 1 presents the current balance sheet for the financial years (FY) 2006-07 to 2010-11. Annexure 2 indicates the cash flow statement of the company for the FY 2004-05 to 2007-08 and 2010-11. The statements since FY2009-2010 relates to Mahindra Satyam. The cash and bank balance figure for FY 2007-08 is Rs. 1,143.10 crores and for the succeeding FY 2008-09 is Rs. 379.10 crores respectively. Similarly the total liabilities FY 2007-08 is 7,381.31 crores and for FY 2008-09 is 1,349.10 crores respectively. The cash flow statement shows the exact figures for operating profit.

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### The Regulatory Reforms ...

Analysts such as Chandna (2010) have brought on the spotlight on the following corporate governance flaws:

- Slack regulatory systems
- Machiavellian promoters and their rampant greed
- Circumspect role of auditors
- Consenting independent directors
- Empowerment of minority investors
- Empowerment of whistle blowers

**Table 4**

#### ***Corporate Governance Initiatives in India - An on-going exercise***

*The Corporate governance initiatives in India have been an ongoing exercise:*

- 1998, the “Desirable Code of Corporate Governance” – a voluntary code was established by the Confederation of Indian Industry(CII)
- The original prescribed regulatory framework for listed companies was instituted by SEBI, termed as Clause 49 of the Listing Agreement.
- 2003,SEBI revised the Clause 49, as per the commendations proposed by the committee.
- October, 2004 SEBI directed further amendment to the Clause 49 on receiving several representations, which were deliberated afresh by the Narayana Murthy Committee.
- 2004, the Indian Government took up a comprehensive assessment of the Companies Act, 1956, which was in its time,a noteworthy milestone in the development of Company Law in India.
- 29<sup>th</sup> August 2008 the Union Cabinet gave its consent for introduction of the Companies Bill, 2008 in the Parliament to alternate the Companies Act, 1956.
- 3<sup>rd</sup> August 2009, The bill was re-introduced as it had lapsed with the dissolution of the house in December 2008.

- *The provisions of Companies Bill are largely considered to be suitable for addressing current issues relating to corporate governance, including those presently seen in the inquiry of the Satyam scam.*
- *The bill has now been re-christened as Companies Bill 2009, and is forwarded to a Parliamentary Standing Committee for commendations. Since the standing committee has set no time frame for presenting its recommendations, the course of the new law is expected to take more than a year.*
- *A revised Companies Bill incorporating the propositions of the Standing Committee is likely to be introduced in the forthcoming Budget session of Parliament...*

*Source: Companies Bill 2008 approved - to replace Companies Act 1956 Legal News India*

Needless to say ,post-Satyam, questions have been raised about the performance and effectiveness of board of directors, the role of auditors, the impact of regulations, the scope of disclosures, etc. Prior to the Satyam scam, India was in the course of revising its 1956 Companies Act , which defines major corporate governance statutes. Post-Satyam this endeavor has gained further momentum. A new corporate governance code, produced by the Ministry of Corporate Affairs aims at enforcing more stringent disclosure obligations, than SEBI presently entails.

The revised Companies Bill, placed before the Standing Committee, is likely to be introduced in the impending Budget session of Parliament .The new code, created by the Ministry of Corporate Affairs, with suggestions prescribed by the Parliamentary Standing Committee, illustrates at various points that the shadow of Satyam hangs over a number of recommendations. We look at the prescriptions presented in the new code as well as SEBI's proposals-on the functioning of independent directors, the enhanced pace of disclosures , conduct of audit and improved transparency in governance mechanisms.

### **Functioning of independent directors**

The new code has several prescriptions relating to stringent norms for the tenure, appointment and conduct of independent directors. The proposals comprise the following:

- ✓ Create a code for conduct of independent directors
- ✓ Institutionalize a system of selection of independent directors drawn from a panel suggested by sectoral and market regulators
- ✓ Ensure an independent board of directors pursuant to Clause 49(e.g., an individual is not independent if he holds 2 per cent of the business or if he is appointed by a family member)
- ✓ Limit the number of directorships one person can hold from the present 15 to 7 boards
- ✓ Appointment of directors on fixed, 6-year contracts and subsequently, having no role in the firm for 3 years, following the contract
- ✓ Independent directors are to be mandatory for both listed and unlisted companies. Currently, independent directors are mandatory for listed companies through clause 49 of the listing agreement and optional for unlisted entities
- ✓ Attach more responsibility and fortify the position of independent directors so that they are able to spot any wrongdoing

- ✓ Ensure remote participation of a director in the board meeting, who cannot be present in person by using a “minuted and signed proceeding of a teleconference or video-conference. This practice would constitute proof of his participation. <sup>i</sup>
- ✓ Mandate due diligence on transactions
- ✓ Increase the personal liability of board members. <sup>ii</sup>
- ✓ Ensure publicly listed firms bear director and executive liability insurance to shield investors from damages

These proposals would enhance the autonomy of the board in the context of the pyramidal structure of Indian family business.

### **Enhanced pace of disclosures**

After the Satyam scam, SEBI has enhanced disclosure compulsions of promoters and controlling investors. They comprise:

- ✓ Controlling shareholders should divulge any share pledges
- ✓ Firms to disclose their balance sheet position twice a year in place of the existing yearly position
- ✓ Firms could present a statement of cash flow along with the balance sheet in its biannual reports
- ✓ Mandate due diligence on transactions even on the part of board members

The improved incidence of disclosure would result in a more robust market check. For instance, shareholders would detect and pressure the board to investigate any irregularities as Satyam's non-interest bearing deposits.

### **Conduct of audit**

SEBI's proposals relating to the conduct of audit as a mechanism for corporate governance requires companies to:

- ✓ Institutionalize independent internal audits(Press Release,2009)
- ✓ Change the external auditor (audit firm) every 5 years to acquire a 'fresh outlook'
- ✓ Rotate audit partner every 3 years
- ✓ Subject audits to a peer assessment
- ✓ Shareholders should endorse terms and conditions of appointment and fee payable to statutory auditors <sup>4</sup>
- ✓ Auditors should not be permitted to limit their liability when there are instances of gross laxity, deception and misconduct on their part

Some of these proposals are already in practice. Major firms in India have begun outsourcing segments of their internal audit to specialized firms. This practice of 'co-sourcing' is performed in the Tatas, Essar, real estate major DLF, Ranbaxy. <sup>5</sup>

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<sup>4</sup> At present ,shareholders solely endorse the appointment of statutory auditors.

<sup>5</sup> It is to be noted that the Bharti group and Hindustan Unilever have conventionally pursued the strategy of outsourcing internal audits. This practice of 'co-sourcing' of internal audits received popularity during the post-Enron scandal in US.

The proposals would evolve on considering all pertinent issues and consequences of execution. For example, the implementation of SEBI's peer review of audit would cause concerns for confidentiality of the financial statements among the peer auditors. Additionally, there is the probability of a conflict of interest with other audits.

### **Improved transparency in governance mechanisms**

The corporate code created by the Ministry of Corporate Affairs as well as SEBI proposals cover different areas of corporate governance. They relate to the distinct separation of the role of Chairman and CEO, institution of a whistleblower policy, adoption of accounting standards, etc.

#### Distinct role of chairman and CEO

- ✓ Recommend listed companies to separate the role and position of chairman and CEO

#### Whistleblower policy

- ✓ Introduce a whistleblower policy for employees to report concerns regarding unethical activities (a policy which is mandatory in the US)
- ✓ Create a law which offers whistleblowers protection for reporting deceitful activity

#### Class-action lawsuits

- ✓ Change securities laws to enable investors to pursue class-action lawsuits against fraudulent players in the company, similar to the US shareholder derivative suit (legal-dictionary.thefreedictionary.com).<sup>iii</sup>

#### Disclosures and accounting standards

- ✓ Revise takeover regulations to augment disclosure in takeovers
- ✓ Adopt International Financial Reporting Standards ("IFRS")
- ✓ Strengthen the SFIO (Serious Frauds Investigation Office) by arming it with legal and statutory powers to investigate corporate irregularities
- ✓ Strengthen shareholder activism
- ✓ Conduct an annual review of internal control effectiveness of the firm

Some of these proposals are on the anvil. In August 2010, the Indian Union Cabinet cleared a bill to shield whistleblowers and punish those revealing the identity of persons disclosing the information. The proposed legislation, Public Interest Disclosure and Protection to Persons Making the Disclosure Bill 2010, endows the Central Vigilance Commission with powers of a civil court to pass stringent penalty to people revealing the identity of whistleblowers. The bill has provisions to thwart victimization or punitive action against whistleblowers (Times of India, 2010).<sup>6</sup>

### **Conclusion**

The Satyam Computer Services Ltd. scandal stunned India (and indeed the world), and demonstrated that improvements in regulations and corporate governance have not kept pace with the country's swift rise in economic and financial clout. The Indian stock market has recouped and Mahindra Satyam lives on.... Civil litigation and criminal indictments carry on against Satyam.

While India's financial reporting standards are high, its prime regulator SEBI is independent of the government and its business press is ardent. However enforcement is weak, loopholes are huge and investor activism passive. These prescriptions for regulatory reform, if and when

implemented, would create a strong regulatory system, but may not always prevent frauds. In spite of the enhanced disclosures and strict risk managing systems in the US, post-Sarbanes Oxley Act, there were no forewarning signs of the imminent Subprime crisis or Madoff's Ponzi scheme. Ultimately it is the integrity and moral principles of the promoters, directors, managers and investors that count and their dedication to institute and follow rigorous governance systems. Satyam seems to be a case of straightforward deceit, rather than a matter of insufficient compliance requirements. It is to be hoped that with the right changes, India can prevent other Satyam-like frauds or check it in the early stages.

While Satyam has become an ongoing saga, the company has received the awards such as the "System Integrator of the year at CNME ICT Achievement Awards 2011" (10th October 2011) and the EMS 2012 Partners Innovation Award (21<sup>st</sup> November 2011).

### End notes

<sup>1</sup> Satyam paradoxically means 'truth' in Sanskrit, an ancient Indian language.

<sup>2</sup> Matyas' is in actual fact, Satyam spelled backwards.

<sup>3</sup> <http://www.moneycontrol.com/financials/satyamcomputerservices/balance-sheet/SCS>

<sup>4</sup> This is in response to Palepu, Satyam's former non-executive director who stated in a written response to Knowledge@Wharton, that he was not present at the board meetings when the Matyas proposals were discussed. Hence under Indian law he was not eligible to vote on the proposals.

<sup>5</sup> This requires listing what kind of offences will be compoundable and what type of offences will result in criminal prosecution.

<sup>6</sup> While the bill will cover central, state and public sector employees; it is a step in the right direction.

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## Annexures

### Annexure 1

	Balance Sheet of Mahindra Satyam				
	----- in Rs. Cr. -----				
	Mar '11	Mar '10	Mar '09	Mar '08	Mar '07
	12 mths	12 mths	12 mths	12 mths	12 mths
<b>Sources Of Funds</b>					
Total Share Capital	235.3	235.2	134.8	134.1	133.44
Equity Share Capital	235.3	235.2	134.8	134.1	133.44
Share Application Money	1,230.40	1,230.50	1,230.40	1.83	7.85
Preference Share Capital	0	0	0	0	0
Reserves	1,925.90	2,061.70	-657.1	7,221.71	5,648.07
Revaluation Reserves	0	0	0	0	0
<b>Net worth</b>	<b>3,391.60</b>	<b>3,527.40</b>	<b>708.1</b>	<b>7,357.64</b>	<b>5,789.36</b>
Secured Loans	31.5	42	641	23.67	13.79

Unsecured Loans	0	0	0	0	0
<b>Total Debt</b>	<b>31.5</b>	<b>42</b>	<b>641</b>	<b>23.67</b>	<b>13.79</b>
<b>Total Liabilities</b>	<b>3,423.10</b>	<b>3,569.40</b>	<b>1,349.10</b>	<b>7,381.31</b>	<b>5,803.15</b>
	<b>Mar '11</b>	<b>Mar '10</b>	<b>Mar '09</b>	<b>Mar '08</b>	<b>Mar '07</b>
	<b>12 mths</b>				
<b>Application Of Funds</b>					
Gross Block	2,020.40	1,818.90	2,155.30	1,486.53	1,280.40
Less: Accum. Depreciation	1,406.70	1,285.90	1,404.40	1,062.04	930.45
<b>Net Block</b>	<b>613.7</b>	<b>533</b>	<b>750.9</b>	<b>424.49</b>	<b>349.95</b>
Capital Work in Progress	268.3	373	389.5	458.63	290.05
<b>Investments</b>	<b>532.1</b>	<b>726.6</b>	<b>93</b>	<b>493.8</b>	<b>201.15</b>
Inventories	59.2	0	1	0	0
Sundry Debtors	1,112.70	850.5	1,467.20	2,223.41	1,649.86
Cash and Bank Balance	421.9	587.7	379.1	1,143.10	593.16
Total Current Assets	1,593.80	1,438.20	1,847.30	3,366.51	2,243.02
Loans and Advances	697.4	850.8	738.9	766.04	394.07
Fixed Deposits	2,227.90	1,504.30	28.5	3,318.58	3,366.66
Total CA, Loans & Advances	4,519.10	3,793.30	2,614.70	7,451.13	6,003.75
Deffered Credit	0	0	0	0	0
Current Liabilities	1,468.60	789	1,290.90	896.46	621.3
Provisions	1,041.50	1,067.50	1,208.10	550.28	420.45
Total CL & Provisions	2,510.10	1,856.50	2,499.00	1,446.74	1,041.75
<b>Net Current Assets</b>	<b>2,009.00</b>	<b>1,936.80</b>	<b>115.7</b>	<b>6,004.39</b>	<b>4,962.00</b>
Miscellaneous Expenses	0	0	0	0	0
<b>Total Assets</b>	<b>3,423.10</b>	<b>3,569.40</b>	<b>1,349.10</b>	<b>7,381.31</b>	<b>5,803.15</b>
Contingent Liabilities	1,365.80	1,581.00	2,350.73	623.28	267.2
Book Value (Rs)	18.37	19.53	-7.75	109.71	86.65

## Annexure 2

<b>Mahindra Satyam</b>					
<b>Cash Flow</b>	----- in Rs. Cr. -----				
	<b>Mar '11</b>	<b>Mar '08</b>	<b>Mar '07</b>	<b>Mar '06</b>	<b>Mar '05</b>
	12 mths	12 mths	12 mths	12 mths	12 mths
<b>Net Profit Before Tax</b>	<b>-73.9</b>	<b>1941.86</b>	<b>1573.23</b>	<b>1332.76</b>	<b>767.12</b>
Net Cash From Operating Activities	-177.2	1412.92	1029.83	785.61	643.96
Net Cash (used in)/from Investing Activities	375.5	-641.22	1678.58	-53.85	-341.18
Net Cash (used in)/from Financing Activities	-19.7	-227.79	34.1	-43.94	-103.57
<b>Net (decrease)/increase In Cash and Cash Equivalents</b>	<b>178.6</b>	<b>501.86</b>	<b>-605.42</b>	<b>689.02</b>	<b>193.9</b>
Opening Cash & Cash Equivalents	253	651.41	1256.83	567.81	373.9
Closing Cash & Cash Equivalents	431.6	1153.27	651.41	1256.83	567.81

<sup>i</sup> This is in response to Palepu, Satyam's former non-executive director who stated in a written response to Knowledge@Wharton, that he was not present at the board meetings when the Matyas proposals were discussed. Hence under Indian law he was not eligible to vote on the proposals.

<sup>ii</sup> This requires listing what kind of offences will be compoundable and what type of offences will result in criminal prosecution.

<sup>iii</sup> A derivative suit is a lawsuit brought by a corporation's shareholders against the firm's board of directors on behalf of the corporation. The suits normally allege gross negligence of the company from its board of directors and ask the court to award the corporation damages.

Source: (<http://legal-dictionary.thefreedictionary.com/Derivative+suit>).

<sup>iiii</sup>

<sup>iii</sup> A derivative suit is a lawsuit brought by a corporation's shareholders against the firm's board of directors on behalf of the corporation. The suits normally allege gross negligence of the company from its board of directors and ask the court to award the corporation damages.

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