Everyone’s getting rich, so why shouldn’t I?

– A common thinking.

CORPORATE FRAUD AND HUMAN PSYCHOLOGY

As per one study it was found that the U.S. organizations lose almost 7 per cent of their revenue due to fraud[1]. Fraud involves intentional acts and is perpetrated by human beings using deception, trickery, and cunning that can be broadly classified as comprising two types of misrepresentation: suggestio falsi (suggestion of falsehood) or suppressio veri (suppression of truth)[2].

Human behaviour is the root cause of fraud. Now behavioural scientists have identified that the fraudsters are industrial psychopaths who applies lying and misrepresentation, the science of persuasion, industrial psychopaths, heuristics and biases in decision making to achieve their dishonest design. From a criminology perspective, white collar crime, like other crime, can best be explained by three factors: a supply of motivated offenders, the availability of suitable targets, and the absence of capable guardians—control systems or someone ‘‘to mind the store’’[3]

Footnotes & References

(1) 2008 Report to the Nation issued by the Association of Certified Fraud Examiners
(2) Sridhar Ramamoorti, Page 522, The Psychology and Sociology of Fraud: Integrating the Behavioral Sciences Component Into Fraud and Forensic Accounting Curricula.
(3) Cohen and Felson, 1979, as written by Sridhar Ramamoorti, Page 524, The Psychology and Sociology of Fraud: Integrating the Behavioral Sciences Component into Fraud and Forensic Accounting Curricula.

The corporate fraudsters are the trust- violators who violate the financial trust in pursuit of the greed for more money. All of the above factors are influenced by the fraudster psychology. After all, personal incentives and perceived pressure drive human behaviour, and the need to rationalize wrongdoing as being somehow defensible is very much psychologically rooted in the notion of cognitive dissonance[1].

WHAT IS CORPORATE GOVERNANCE

Corporate governance is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders' role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board's actions are subject to laws, regulations and the shareholders in general meeting[2].

Footnotes & References

(1) ***Sridhar Ramamoorti, Page 525, The Psychology and Sociology of Fraud: Integrating the Behavioral Sciences Component Into Fraud and Forensic Accounting Curricula.***

(2) ***This classic definition of "Corporate Governance" as provided by the Uk Cadbury Committee Report on Corporate Governance, 1992 which still holds good and still retained by the Code of Corporate Governance, 2010 of UK.***

CORPORATE GOVERNANCE AND SOCIETY

In the present set up the impact of a white collar crime is not merely confined to a particular company but it is a global phenomenon. The high profile frauds are generally a team sport, the impact of which is felt to deepest of socio – economic structure. The breakdown of corporate governance function has a wider ramification than it could be ever thought of. Recently the world has seen how the collapse of Enron and WorldCom shaken the economy and credibility of USA corporate structure. The failure of these companies has been attributable to the fraud and negligence of the board of directors of the companies. The ripples of the collapse of these mega companies were felt not only the stakeholders of the companies but it was felt to the deepest of the national and international economies given the pervasive equity culture prevailed in America. A state of recession was feared in Europe and Asian countries as America was their largest trading partner. Hence it will be a very narrow view to see the board of a public company as merely a group of persons who are responsible to run a company in a legal way but it should be seen as a **complex social unit**. This feature of the board casts a higher degree of care and duty on it to act fairly and honestly in the contemporary corporate culture.

Hence, an effective model of corporate governance is imperative for a peaceful and stable society.

Agency Problem and the need of the Board of Directors

A proper and just functioning of Board of Directors is considered to be the most essential feature of the corporate governance. For the fulfilment of corporate governance requirement it is imperative that the board of the company should furnish its agency functions properly. Separation of ownership and management is the most unique feature of the today's corporate structure. The ownership of the company is widely dispersed in the form of innumerable scattered shareholders whereas given the large size of the company it becomes necessary that it be run by the specialised group of persons who have expertise in managing the companies. Hence, the company is managed by a centralised board containing such specialised persons which is the Board of Directors (BOD), which contains the shareholders (owners) as well, who are supposed to work in the best interest of the shareholders and company as a whole and not in their own best interest. This situation is popularly known as the "agency problem". The study of agency problem attempts to control conflicts of interest among corporate constituencies.

It may happen that the Board may not work in the best interest of the owners and work in the interest of itself. This "managerial agency problem" has the most prominently aspects as moral hazard or competence problem among the members of the board. A successful corporate governance model is primarily essential in order to deal with this agency problem which ensures that there is no moral or competence problem in the board, and the administration of the company could run smoothly.

INDEPENDENT DIRECTOR, THEIR ROLE IN THE BOARD COMMITTEES AND CORPORATE GOVERNANCE

As we have seen above, a proper functioning Board of a company is the prerequisite of a successful corporate governance model as the managerial agency function is exclusively conferred to the Board of Director. Post-Enron, in light of the corporate difficulties in the United States, the issue of good corporate governance has once again been brought to the forefront[1]. Virtually, the turn of the century witnessed a proliferation of independent directors beyond the borders of the U.S. and the U.K. to several other countries around the world. This is due to the profound impact that corporate governance reforms (culminating with the Sarbanes-Oxley Act in the U.S. and the Cadbury Committee Report in the U.K.) have had on corporate governance norms-making around the world, particularly in relation to the appointment of independent directors as an essential matter of good governance[2]. In the United States, the New York Stock Exchange ("NYSE") Corporate Accountability and Listing Standards Committee submitted a report to enhance the corporate governance standard. The report makes recommendations to amend the NYSE's listing standards with the goal of enhancing the accountability, integrity and transparency of the NYSE's listed companies and was accepted by NYSE Board of Directors on 1 August 2002. It was felt in the recommendation that independent directors would act as a check on a corporation's management and at the same time protect the interests of shareholders of the corporation[3].

Footnotes & References

(1) See, e.g. "Designed by Committee", Economist, 15 June 2002, 70 (Special Report on Corporate Governance)

(2) Umakanth Varottil, at Page 3, EVOLUTION AND EFFECTIVENESS OF INDEPENDENT DIRECTORS IN INDIAN CORPORAT GOVERNANCE.TAN Cheng Han, at Page 1, CORPORATE GOVERNANCE AFTER ENRON

http://www.fetp.edu.vn/events/theFilename/LawReadings/L4e.pdf

There is a near consensus among the policy maker that the agency problem could be sorted out by ensuring more participation of the independent directors into the board committees. Klein (1995) examines the committee structure of boards and the directors' roles within these committees. She finds that committee structures with specialized roles enhance the board's productivity and its efficiency in monitoring. Recent reforms have stressed on the board having the majority of independent director as well as their participations in the key board committees. For the purpose of fulfilling the monitory functions the board can have various committees such as audit committee, nomination committee, compensation committee, risk committee, special committee etc.

Who are Independent Directors?

The genesis of independent directors could be found in 1950s when the Delaware companies in USA voluntarily included independent directors much before the same was required by law. Realising their importance the Delaware court and stock exchanges started making a great stress on the institution of independent directors. Having independent directors, at least in theory, minimizes the danger of management abusing their power[1].

Footnotes & References

(1) As observed by TAN Cheng Han, at Page 2, CORPORATE GOVERNANCE AFTER ENRON http://www.fetp.edu.vn/events/theFilename/LawReadings/L4e.pdf

After the 1990s the institution of independent directors was settled in the field of corporate governance area due to the spate of recommendations in UK & US (such as Cadbury Committee Report on Corporate Governance, 1992 or BLUE RIBBON COMMITTEE ON IMPROVING THE EFFECTIVENESS OF CORPORATE AUDIT COMMITTEES (1999) in USA etc.) in which the reliance was placed on the independent director as an essential element to enhance the standard of corporate governance. Following the Enron debacles, independent directors were recognized by statute as well. Independent directors are a sub-set of non-executive directors[1].

NYSE LISTED COMPANY MANUAL laid down that a director is an independent director who has no material relationship with the company or he is not in employment with such company[2]. The Sarbanes-Oxley Act defines an "independent" director as one who does not accept any other compensation from the issuer except in his or her capacity as a member of the audit committee, or another board committee.

The Delaware Court of Chancery in the case of In re ORACLE CORP DERIVATIVE LITIGATION[3], relied on the following definition in order to determine whether the director was independent or not '''Independent director' means a person other than an officer or employee of the company or its subsidiaries or any other individual having a relationship, which, in the opinion of the company's

Footnotes & References

(1) Umakanth Varottil, at Page 28, EVOLUTION AND EFFECTIVENESS OF INDEPENDENT DIRECTORS IN INDIAN CORPORAT GOVERNANCE.

(2) Section 303A.01, NYSE LISTED COMPANY MANUAL.

(3) 824 A.2d 917.

board of directors, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director.’’

Different Acts or different courts may have the variation of definitions to define the independent directors but the basic feature of an independent director lies in the fact that they are not affiliated to the executive function of the company, i.e. they have no material relation with the day to day business of the company.

Independent Director and his Role in the Board of a company

Now, UK Companies Act, 2006[1] provides that “a director of the company must exercise independent judgment. In the recent trend of corporate governance it has been generally accepted that the introduction of the independent director in the Board is underpinned by the fact that a Board containing more number of independent director will ensure a higher standard of corporate governance. In consequence the corporate governance code and listing guidelines of Australia, USA and UK provide that the majority of the Board of Directors must be independent Directors. The requirement is not same in the Asian Countries but Singapore Council of Corporate Governance, 2011 proposed that the independent directors should constitute at least half of the Board where the chairman and the CEO of the Board is the same person or they are the family members, or where the chairman is not an independent director or he is the part of the management team.

Footnotes & References

(1) Sec. 173(1) of UK Companies Act, 2006)

Monitoring Role of Independent Directors

One of the roles of independent directors is to monitor management. Independent directors are intended to protect the interests of shareholders through their monitoring function. Independent directors are directors who are not affiliated to executive or inside directors. In addition, independent directors should also generally be the persons who do not have a business or other relationship with the company or with other senior officers of the company. With reference to independent directors, Dahya and McConnell find that during the 1990s and beyond, “at least 26 countries have witnessed publication of guidelines that stipulate minimum levels for the representation of outside directors on boards of publicly traded companies[1].”

In the case of United States and United Kingdom there has been near unanimous support in favour of the independent directorship for achieving a higher standard of corporate governance where the large public company has diffused shareholding pattern.

Sarbanes-Oxley Act and Independent Director

Sarbanes – Oxley Act (SOX) was passed in the aftermath of the rampant scandals involving fraud and mismanagement at such major U.S. companies as

Footnotes & References

(1) ***Jay Dahya & John J. McConnell, Board Composition, Corporate Performance, and the Cadbury Committee Recommendation (2005), available at http://ssrn.com/abstract=687429, at 1***

Enron, Tyco, Adelphia, and WorldCom. In this Act a special reliance was placed on the independent directors to enhance the standard of corporate governance. The wave of corporate governance reforms was led by the enactment of the Sarbanes-Oxley Act and revisions to the listing rules of NYSE and NASDAQ that introduced mandatory board composition requirements for the first time[1].

The Sarbanes-Oxley Act defines an "independent" director for this purpose as one who, except in his or her capacity as a member of the audit committee, another board committee or the board:

(1) does not accept any consulting, advisory or other compensation from the issuer; and
(2) He is not an affiliated person, as defined by the 1940 Act, of the issuer or its subsidiaries.

Title III confers extra - ordinary obligations on public companies for financial reports and to ensure independence and responsibilities audit committee. The audit committee required appointing and overseeing the performance of the company's auditors, and the auditors required to report to the audit committee. Audit committee members constituted the board of directors

Footnotes & References

(1)***Umakanth Varottil, at Page 24, EVOLUTION AND EFFECTIVENESS OF INDEPENDENT DIRECTORS IN INDIAN CORPORAT GOVERNANCE).***

This remained independent (other than serving on the board of directors and the board's committees).

Section 301 of Title III conferred extra ordinary function for assisting directors of public companies and to fulfil their responsibilities to shareholders, regulators, and the public. It was empowered to hire outside counsel and experts at the company's expense and in its sole discretion. Consequently, outside experts and lawyers were employed by the audit committees of boards of public companies in a variety of issues.

Listing Rules of NYSE and NASDAQ Stock Exchanges

It is also to be noted that in the revised rules of the NYSE and NASDAQ also require that all listed companies in these exchanges must contain the boards with a majority of independent directors. A director does not qualify as independent unless the board affirmatively determines that the director has no material relationship with the listed company[1]. NYSE LISTED COMPANY MANUAL laid down the following tests (303A.01 Independent Directors) to determine whether a director is independent or not. No director qualifies as "independent" unless the board of directors

Footnotes & References

(1) ***Umakanth Varottil, at Page 24, EVOLUTION AND EFFECTIVENESS OF INDEPENDENT DIRECTORS IN INDIAN CORPORAT GOVERNANCE.***

affirmatively determines that the director has no material relationship with the listed company or employment by the individual or family member with the listed company as an executive officer within the last three years;

(i) receipt by the individual or a family member of compensation from the company of certain specified amounts;

(ii) association with a firm that is the Company's internal or external auditor;

(iii) employment as an executive officer of another company where any of the listed company's present executive officers serve on that company's compensation committee;

(iv) Employment as executive officer of a company that has payment transactions with the listed company for property or services in an amount which is beyond a specified amount[1].

Both the exchanges exempt controlled companies from provisions mandating independent directors. This is explicit recognition of the fact that independent directors are a solution to the agency problem between managers and shareholders[1].

Footnotes & References

(1) Umakanth Varottil, at Page 25, EVOLUTION AND EFFECTIVENESS OF INDEPENDENT DIRECTORS IN INDIAN CORPORAT GOVERNANCE.

Cadbury Committee Report

This report was made by a committee chaired by Sir Adrian Cadbury, which was a response to major corporate frauds (such as BCCI, Robert Maxwell etc. related with corporate governance failures in the UK. The Cadbury Committee Report introduced the concepts of non-executive director and independent director in UK corporate governance law. The Cadbury Committee Report assigns two major responsibilities to non-executive directors. It provides –

Non-executive directors have two particularly important contributions to make to the governance process of the board.

(i) To review the performance of the board and the executives; and
(ii) The second is in taking the lead where potential conflicts of interest arise.[1].

These powers have been conferred to the non – executive directors in furtherance with their monitoring function of the board and to sort out the manager shareholder agency problem.

An important aspect of effective corporate governance is the recognition that the specific interests of the executive management and the wider interests of the company may at times diverge, for example over takeovers, boardroom succession, or directors' pay. Independent non- executive - directors, whose interests are less directly affected, are well-placed to help to resolve such situations[2].

Footnotes & References

(1) Cadbury Committee Report Para 4.4-4.6.

(2) Cadbury Committee Report 4.6.

To meet the recommendations on the composition of sub-committees of the board, all boards will require a minimum of three non-executive directors, one of whom may be the chairman of the company provided he or she is not also its executive head[1].

UK Corporate Governance code, 2010

The Cadbury Committee Report is considered as the first leap of UK for formulating the rules for the corporate governance. In 2010 UK passed the Corporate Governance code, 2010 (formerly known as Combined Code) which was actually the consolidation and refinement of so many reports including the Cadbury Committee Report which were passed earlier. It provided the set of rules of good governance for the companies which are listed in the London Stock Exchange. Like the other codes for corporate governance this code also relies upon the role of independent directors to enhance the standard of corporate governance. In its Section B.1 - Main Principles of the Code it deals with effectiveness. It provides, "the board and its committees should have the appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively. The board should include an appropriate

Footnotes & References

(1) Cadbury Committee Report 4.11

combination of executive and non-executive directors (and, in particular, independent non-executive directors) such that no individual or small group of individuals can dominate the board's decision taking". It further provides, "The board should appoint one of the independent non-executive directors to be the senior independent director to provide a sounding board for the chairman and to serve as an intermediary for the other directors when necessary". (A.4.1 Code Provisions).

In A.4.2, Code Provisions it confers the monitoring function on the senior independent director. It provides the chairman should hold meetings with the non-executive directors without the executives present. Led by the senior independent director, the non-executive directors should meet without the chairman present at least annually to appraise the chairman's performance and on such other occasions as are deemed appropriate. Further, B.6.3 Code Provisions, the non-executive directors, led by the senior independent director, should be responsible for performance evaluation of the chairman, taking into account the views of executive directors.

In B.1.2, Code Provisions, it provides, except for smaller companies, at least half the board, excluding the chairman, should comprise non-executive directors determined by the board to be independent. A smaller company should have at least two independent non-executive directors.

Independent Directors in Singapore -

Under the Companies Act, 1967 of Singapore there is no mention of independent directors except in section 201B, which relates to the constitution of audit committees of listed companies. The independent director was defined in Guidance Notes 2.1 of REPORT OF THE CORPORATE GOVERNANCE

COMMITTEE, 2001 and gives stress on the director's independence - There should be a strong and independent element on the Board, with independent directors making up at least one-third of the Board. An "independent" director is one who has no relationship with the company, its related companies or its officers that could interfere, or be reasonably perceived to interfere, with the exercise of the director's independent business judgement with a view to the best interests of the company.

Final Recommendations on the Director's Independence on the Proposed Revisions to the Code of Corporate Governance[1] –

1. Relationship with Substantial Shareholders

The Council recommends tightening the definition of director independence such that a director who is a substantial shareholder, or an immediate family member of a substantial shareholder, or is/was directly associated with a substantial shareholder in the current or any of the past 3 years would be considered non-independent.

2. 9 Year Period for Board Service

The Council recommends that the independence of any director who had served on the Board beyond nine years from the date of his appointment should be subject to particularly rigorous review, and the Board should explain why any such director should be considered independent.

Footnotes & References

(1) Final Recommendations on the Proposed Revisions to the Code of Corporate Governance (Media Release as on 22 November 2011).

(3) Relationships with External Organisations

The Council recommends to include, as a factor affecting a director's independence, whether the director, in the current or immediate past financial year, is or was, a substantial shareholder, partner, executive officer, or director of any organisation to/from which the company or its subsidiaries made/receive significant payments or material services in the current or immediate past financial year.

Board Committees

The board of a company is the group of directors who are responsible for the fairness and performance of the company though it delegates certain power and functions to the committees containing the group of directors to confer those specific functions. Appropriate structures for these delegations are kept in places which are accompanied by monitoring and reporting systems. Monitoring functions of the board is the most important features for the corporate governance requirement. In order to fulfil the corporate social responsibility of the company it is necessary that all the organs of the companies are kept under the watch so that it function fraud free. In the country like China and Germany, the public companies have two tier boards for the purpose of furnishing the executive and monitoring functions. But the same is not the case for the countries like UK, US and Singapore. The board of these countries furnish the monitoring function by devising the committees like audit committee, compensation committee nomination committee, risk committee etc. The law also allows the public listed companies to make subcommittees like donation committees, investment committees etc. so that a proper allocation of work can be made between the teams.

A company can have many committees and sub - committees but the most important committees are -

(1) Audit Committee[1] - The audit committee is established with the aim of enhancing confidence in the integrity of an organisation's processes and procedures relating to internal control and corporate reporting including financial reporting. Among many responsibilities the boards entrust the Audit Committee with are the transparency and accuracy of financial reporting and disclosures, effectiveness of external and internal audit functions.

(2) Nomination Committee – The primary duty of the nomination committee of a company is to focus on evaluating and examining the skills and speciality which are needed for the suitable candidates for various director positions.

(3) Compensation Committee - The primary duty of the compensation committee of a company is to focus on reviewing and approving the compensations allowed to the CEOs, chairman and other officers of the company.

Footnotes & References

(1) As defined in http://www.corpgov.deloitte.com/site/in/audit-committee/

Board Committees Under the UK Corporate Governance Code, 2010

The UK Corporate Governance Code requires a board to have three committees: Remuneration Committee, Audit Committee and Nomination Committee. The Code also requires that the all of these three committees should have the terms of reference and for the purpose of scrutiny these should be available to the public at large.

Audit Committee

Part C.3 of the Corporate Governance Code, 2010 deals with the Audit Committee and its role and functions. In C.3.1, Code Provisions, it provides, the board should establish an audit committee of at least three, or in the case of smaller companies two, independent non-executive directors. In smaller companies the company chairman may be a member of, but not chair, the committee in addition to the independent non-executive directors, provided he or she was considered independent on appointment as chairman.

The main role and responsibilities of the audit committee should be to set out in written terms of reference, to monitor and review the effectiveness of the company's internal audit function and should include monitoring the integrity of the financial statements of the company (C.3.2, Code Provision). It is also conferred with the responsibility to review the company's internal control and risk management systems unless expressly addressed by a separate board **Risk Committee** composed of independent directors, or by the board itself.

Remuneration Committee

In D.2.1, Code Provision provides, the board should establish a remuneration committee of at least three, or in the case of smaller companies' two, independent non-executive directors. In addition the company chairman may also be a member of, but not chair, the committee if he or she was considered independent on appointment as chairman. The remuneration committee is delegated a responsibility for setting remuneration for all executive directors and the chairman, including pension rights and any compensation payments (D.2.1, Code Provision).

SCHEDULE A of the Code provides that the remuneration committee should consider whether the directors should be eligible for annual bonuses. If so, performance conditions should be relevant, stretching and designed to promote the long-term success of the company.

Nomination Committee

B.2.1 Code Provision - There should be a nomination committee which should lead the process for board appointments and make recommendations to the board. A majority of members of the nomination committee should be independent non-executive directors. The chairman or an independent non-executive director should chair the committee, but the chairman should not chair the nomination committee when it is dealing with the appointment of a successor to the chairmanship.

B.2.2, Code Provision, further provides, the nomination committee should evaluate the balance of skills, experience, independence and knowledge on the board and, in the light of this evaluation, prepare a description of the role and capabilities required for a particular appointment.

Board Committee in United States

Under Sarbanes-Oxley Act

As discussed above the Sarbanes–Oxley Act was passed in the aftermath of great corporate debacles of USA. Hence, the Sarbanes-Oxley Act (SOX) attempts to regulate the code of conduct of the board of directors to avoid such failure of corporate governance once again. The act has no substantial effect on the directors' independence but affects in the area of audit committee.

Section 301 of SOX further regulates the audit committee. SOX § 301, the power to hire, fire, and compensate the external auditors must reside in the company's audit committee, as opposed to the management or the board of directors as a whole. New rules also require that all members of the audit committee be "independent," and the new definitions of independence are stricter than past conceptions of independence[1].

As previously noted, new rules put the power to hire and compensate external auditors in audit committees composed entirely of independent directors, as a way of reducing conflicting pressures. But they also seek to increase the

Footnotes & References

(1) Robert Charles Clark, Page 10, Corporate Governance Changes in the Wake of the Sarbanes-Oxley Act: A Morality Tale for Policymakers Too.

chance that the committees will monitor well and effectively, by requiring that all of a company's committee members be financially literate and by encouraging the company (via a disclosure requirement) to have at least one financial expert on the committee[1].

It mandates the corporate to have a majority of independent directors in the board. Simultaneously, it requires the key board committees - audits, executive compensation, and nomination of new directors – composed entirely of independent directors. In order to be considered to be independent for purposes of being a member of an audit committee of an issuer may not, other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee—

(i) accept any consulting, advisory, or other compensatory fee from the issuer;

(ii) Be an affiliated person of the issuer or any subsidiary thereof[2].

As can be seen, the NYSE's former rules were more flexible than those of the

Footnotes & References

(1) Robert Charles Clark, Page 12, Corporate Governance Changes in the Wake of the Sarbanes-Oxley Act: A Morality Tale for Policymakers Too.

(2) Sarbanes-Oxley Act of 2002 § 301 (codified at 15 U.S.C. § 78j-1(m) (3) (B).

SOA, allowing the board in many circumstances to waive presumptive bars to independence.[1] Like SOX the NYCG Rules also contemplate that the board should consists of majority of independent directors and thus, the company cannot simply relegate the task of appointing the new director to the entire board which would obviously contain the insiders like director and chairman. Like SOX, the NYCG also requires for every public company to have three committees, audit, compensation and nomination, committees. This any other situation would give rise to fraud and other problems. The above rules of NYCG also oblige all the public companies to have a written charter of all the power and duties for the committees.

Under Section 952, Corporate Governance Provisions of Dodd-Frank also mandates that the compensation committees of reporting companies must be fully independent. Section 952 makes a number of provisions relating to compensation committee. For example, it provides that the SEC should prohibit the self-regulatory organizations i.e., stock exchanges and NASDAQ from listing any issuer that does not comply with specified requirements relating to the independence of compensation committee members.

<u>Footnotes & References</u>

(1) ***as observed by DONALD C. CLARKE, Page 87, THREE CONCEPTS OF THE INDEPENDENT DIRECTOR.***

Conclusion

The recent experience has also shown that merely ensuring the directors independence and forming the board committees does not guarantee the best corporate governance. Even though, it enhances the general standard of corporate governance.

It is not a surprise that there is a lining of negative views exist in the system which raises the question of efficacy of independent board committees consisting the independent directors. Independent directors are in the part time job in the company and they don't actively participate in the executive function of the company. Their knowledge and efficacy is always under the question given the fact that they are not sufficiently informed. Their access to information may be controlled by the full time executive of the company. The independent director of the company may feel themselves under pressure to raise any issue against the CEOs and chairman of the company if the shares price is soaring as the price of the shares considered as the key performance metric. A study by April Klein[1] finds that audit, nomination, and compensation

Footnotes & References –

(1) April Klein, Firm Performance and Board Committee Structure, 41 J.L. & ECON. 275 (1998).

committees, traditionally dominated by outsiders, have little, if any, effect on firm performance regardless of how those committees are staffed. Indeed, in direct contrast to conventional wisdom, Klein found a positive correlation between firm performance and the presence of insiders on a board's finance and investment committees. It is not an exaggeration to say that the concept and usefulness of the independent directors are remained unexamined.

Enron had a proper audit committee operating under the SEC's expanded rules on audit committee disclosure and headed by learned accounting experts but still the failure of the company had made a historical failure of corporate governance.

A more diversified company management structure, containing both the executive and independent director, is definitely desirable for the public listed company for the purpose of delivering good corporate governance and to avoid the Enron like problems. But the fact remains that law can devise control and system of staffing but human behaviour and honesty cannot be legislated.